

Central Intelligence Agency



Washington, D.C. 20505

14 February 2014

Mr. Trevor Griffey  
P.O. Box 45044  
Seattle, WA 98145

Reference: F-2014-00786

Dear Mr. Griffey:

This is a final response to your 31 January 2014 Freedom of Information Act request, received in the office of the Information and Privacy Coordinator on 6 February 2014, for a copy of the document titled "Internal Audit of the Central Intelligence Agency, 1947 - 67," completed in December 1972.

We conducted a search of our system of previously released documents and located the enclosed document you requested, consisting of 122 pages. Please be advised that this document was released as part of another release program. Because you are entitled to the first 100 pages free, there is no charge for processing your request because the remaining amount would be minimal.

Sincerely,

A handwritten signature in black ink, appearing to read "Michele Meeks".

Michele Meeks  
Information and Privacy Coordinator

Enclosure

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EO 13526 3.3(b)(1)>25Yrs  
EO 13526 3.3(b)(6)>25Yrs  
EO 13526 3.5(c)

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# The DCI Historical Series

INTERNAL AUDIT OF THE CENTRAL INTELLIGENCE AGENCY  
1947 THROUGH 1967

~~Secret~~

DCI-5

December 1972

Copy 3 of 3

## W A R N I N G

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THE DCI HISTORICAL SERIES

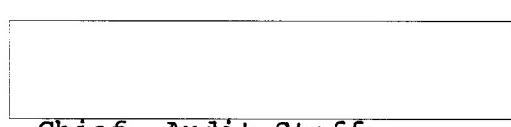
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INTERNAL AUDIT OF THE CENTRAL INTELLIGENCE AGENCY  
1947 THROUGH 1967

by



December 1972



Chief, Audit Staff

HISTORICAL STAFF  
CENTRAL INTELLIGENCE AGENCY

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	<u>Page</u>
Foreword . . . . .	iii
I. The Formative Years, 1947-51 . . . . .	1
II. Changing Concepts, 1951-52 . . . . .	10
III. The Expanding Scope of Audit, 1952-59 .	16
IV. Audit of Voucherized Funds, 1959-60 . . .	54
V. Comprehensive Audit of Agency Activities, 1960-67 . . . . .	59
VI. Synopsis . . . . .	97

Appendices

A. Chronology, 1947-67 . . . . .	101
B. Source References . . . . .	104

Illustrations

Figure 1. Organization Chart - 1953 . . . . .	30
Figure 2. Organization Chart - 1954 . . . . .	31
Figure 3. Organization Chart - 1961 . . . . .	61
Figure 4. Audit Report Cover Sheet . . . . .	64
Figure 5. Organization Chart - 1967 . . . . .	99

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The Central Intelligence Act of 1949 grants the Director of Central Intelligence the authority to expend sums made available to the Agency without regard to the provisions of law and regulations relating to the expenditure of Government funds over his certification that such expenditures are of a confidential, extraordinary, or emergency nature. Funds to be accounted for on the basis of this certification are known as unvouchered or confidential funds.

This authority places unusual responsibility on the Director to assure that confidential fund expenditures are meticulously supervised and controlled in such a manner as to prevent any misuse of funds or services and supplies procured with these funds which could conceivably lead to Congressional withdrawal of the confidential funds authority. The mechanisms and procedures necessary to achieve this control are established in a variety of regulatory and procedural issuances

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which, in application, provide effective checks and balances to ensure authorized and proper custody and use of Agency assets. A continuous monitoring of the application and effectiveness of procedures and controls so established is the mission of the Audit Staff of the Office of the Inspector General.

The Chief, Audit Staff is responsible for performing final independent audits annually, or as often as he deems necessary, of all Agency activities, including Headquarters components, proprietary and other projects, and domestic and overseas field installations. These audits include the review and appraisal of policies, procedures, and practices as considered necessary by the Chief, Audit Staff to ascertain that controls and records are adequate to assure the proper safeguarding of, use of, and accounting for Agency assets; and to verify compliance with applicable law, policies, regulations, and procedures.

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The results of audits are reported to appropriate Agency offices for corrective action and to the Director through the Inspector General. The Audit Staff is also required to report any activities which are found, as a result of audit, to be uneconomical, inefficient, or improper. Through the media of these reports the Director and Agency management are apprised of the application and effectiveness of existing regulatory controls and of areas potentially in need of new or improved controls. While the influence of the Audit Staff is most dramatically presented in the above-described function as an extension of top management, the broader value of the Staff is to be found in its influence on lower management and working levels. In the conduct of audits, Staff auditors inculcate principles of sound financial control and management at all levels both formally and informally, thus expanding the base of interest in good management practice throughout the Agency. The effectiveness of the Audit Staff in the per-

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formance of the foregoing mission may have been foreseen by early Agency managers when the independent audit service was initiated, but in practice the organization of the Staff as well as its professional techniques and effectiveness have evolved through more than twenty years of prudent management.

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INTERNAL AUDIT OF THE  
CENTRAL INTELLIGENCE AGENCY 1947 THROUGH 1967

I. The Formative Years, 1947-51

A facility for the independent audit of confidential funds existed from the days of the Central Intelligence Group, the immediate antecedent of the Agency. In CIG General Order Number 3, dated 1 July 1947, an independent Executive for Inspection and Security was established "to provide overall inspection, audit and security...".<sup>1/\*</sup> The CIA Organization Chart of 15 October 1947 places the Audit Division in the Inspection and Audit Branch of the Executive for Inspection and Security. The first professional auditor, [redacted] entered on duty 16 November 1947,\*\* and by November 1948 the Division, having expanded to a

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\*For serially numbered source references, see Appendix B.

[redacted] retired in 1963.

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strength of [ ] professional and clerical employees, was designated the Audit Branch.<sup>2/</sup>

Authority and specific directives for the conduct of the initial audit of confidential funds accounts were transmitted from the Director of Central Intelligence, Rear Admiral Roscoe H.

Hillenkoetter, by memorandum dated 16 December

1947.<sup>3/</sup> Security of operations was emphasized in these instructions, and the Director required that audit of the confidential funds accounts of the Office of Special Operations (OSO) was to be by the Chief, Audit Branch only. This emphasis on security was repeated in a supplemental memorandum dated 9 November 1948<sup>4/</sup> and in subsequent audit instructions dated 6 June 1949.<sup>5/</sup> Only three copies of the first audit report of transactions of the Special Funds Division\* were distributed,<sup>6/</sup>

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\*Special Funds Division was the finance and disbursing component of OSO for confidential or unvouchered funds. This component later formed the nucleus of the Finance Division of the Office of the Comptroller.

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one to the Director, one to the Executive, and one to the Budget Officer, and these, as well as all other related correspondence, were classified TOP SECRET.

Traditional governmental audit processes prior to 1950 were mainly concerned with verification of accounts, review of custodial practices, and the examination of vouchers recording expenditures. Early Agency auditors, proceeding from prior experience with other government agencies (notably the Department of Agriculture), applied these audit processes to confidential funds.

Detailed review of vouchers was emphasized and all transactions were examined for proper approval and certification, compliance with such standard legal and regulatory requirements as were applicable, adequate supporting documentation, mathematical accuracy, and correct accounting distribution.

In October 1950, responsibility for audit of Agency property and supply accounts was assigned to Audit Division and similar audit principles to

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those described above were applied.<sup>7/</sup> Detailed reviews were made of property accounts and vouchered property transactions, and extensive physical inventories were conducted. The establishment of effective accounting records and of standard financial and logistical management criteria became the first priority of the Audit Division. Much time and effort was spent in assisting financial and logistical management in the formulation of accounting procedures and in the actual preparation of vouchers and the maintenance of accounts. These audit processes, while cumbersome and time consuming, served a function and were effective in focusing the attention of Agency management on the essential requirements for internal control and effective accounting and management procedures which were later formalized as Agency regulations or directives.

The first audit report covering confidential

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funds expenditures by the Special Funds Division\* for the period 20 October 1946 to 31 December 1947 was released on 31 May 1949. The audit was conducted in conformance with processes described above. The report contained 68 findings ranging in importance from failure to make year-end adjustments between current and prospective fiscal year appropriations to the notation of several minor arithmetic errors. Approximately 75 percent of the matters reported pertained to inaccuracies in the computation of claims for transportation and per diem of employees en route to or from overseas posts.<sup>8/</sup> Many of these findings were developed through utilization of the Standardized Government Travel Regulations (SGTR's) promulgated by the Bureau of the Budget as audit criteria, although these regulations were not in effect in the Agency at the time the travel vouchers were processed and certified. This ex post facto approach to audit met

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\*See footnote, p.2, above.

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with some justifiable criticism, but the SGTR's were adopted for Agency use before the release of the audit report, which emphasized the need for management standards in this area. If other than administrative expenses were audited, related findings were not reflected in the report.

The reception of the report by the Agency administration was generally favorable, and the constructive nature of the audit recommendations was noted. The most severe criticism by both the CIA Executive and the Budget Officer was that the report was so delayed in release that timely corrective action to controls and procedures was not possible.<sup>9/</sup> This failing persisted, and a subsequent report of the audit of confidential funds disbursements and accounts for the period 1 July 1949 through 31 December 1950 was not released until 27 February 1952.<sup>10/</sup> Some improvement was made with an audit of confidential funds disbursements and accounts relating to the Office for Policy Coordination (OPC) for the period 1 July

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1949 through 31 December 1950, which was completed and released within about six months of the audit date.11/

Routine delays in releasing audit reports continued to some extent until about 1954. Reasons offered for the delays included shortages of audit personnel and incomplete accounting records. Certainly a part of the fault must have been attributable to the personal involvement of the Chief Auditor in the conduct of audits, which may have distracted him from his primary responsibility for the review and release of reports. The personnel shortage was alleviated by an increase in the Audit Division Table of Organization (T/O). By early 1951 the on-duty strength of the Audit Division was  professional and clerical employees against an authorized strength of  positions. By January 1952 the on-duty strength was  12/ and one year later was  13/. Improvement in accounting records and of financial accounting procedures in general was initiated by a task force appointed by the

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Assistant Deputy Director for Administration. In the memorandum advising Agency executives of this task force,<sup>14/</sup> the ADDA observed that review of the last report of audit disclosed a large number of procedural questions which urgently needed resolution and that this resolution was necessary both to provide operators with needful policy and procedural guidance as well as to adequately protect the Agency in the highly important matter of handling money.

Lieutenant General Walter Bedell Smith, soon after replacing Rear Admiral Hillenkoetter as Director of Central Intelligence on 7 October 1950, began to reorganize the Agency into functional Deputy Directorates. Administrative functions formerly assigned to the CIA Executive were transferred beginning in December 1950 to the newly designated Deputy Director for Administration (DDA), who also absorbed the previously independent support elements of OSO and OPC. In connection with this general reorganization, the Executive for

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Inspection and Security, including the Audit Division, was redesignated the Inspection and Security (I&S) Staff of the Office of the Director of Central Intelligence. Later, in April 1951, the Audit Division was transferred from the I&S Staff to the DDA where it became the Audit Office.<sup>15/</sup> With this transfer the Auditor achieved senior staff status and a position of potential authority.

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## II. Changing Concepts, 1951-52

As noted previously, government audit procedures traditionally required examination of all expenditure vouchers. This requirement was established by the Budgetary and Accounting Act of 1921 (31 USC 71) which provided that

All claims and demands whatever by the Government of the United States, or against it, and all accounts whatever in which the Government of the United States is concerned... shall be settled in the General Accounting Office.

In 1949 the Commission on Organization of the Executive Branch of the Government (The Hoover Commission) noted that this practice was highly inefficient and recommended that it be stopped.

In lieu of this procedure, the Commission recommended substitution of a

spot sampling process at various places where the expenditure vouchers and papers are administratively checked... .

The Congress acted on this recommendation in the

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Accounting and Auditing Act of 1950 (31 USC 65) by providing that

The auditing for the Government, conducted by the Comptroller General of the United States as an agent of the Congress be directed at determining the extent to which accounting and related financial reporting fulfill the purposes specified, financial transactions have been consummated in accordance with laws, regulations, or other legal requirements, and adequate internal financial control over operations is exercised.

In July 1951 [redacted]

[redacted] was appointed as financial advisor

to the DDA to study and evaluate the organization and utilization of Agency covert audit facilities in the context of the foregoing changes in governmental audit procedures. In his report to the DDA, dated 20 August 1951,<sup>16/</sup> [redacted] identified the function of the Agency audit of confidential funds as being in lieu of audit by the General Accounting Office of normal governmental departments. In furtherance of this concept, he recommended a substantial increase in the degree of administrative

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review of expenditure vouchers by the Finance Division prior to certification for payment. He further recommended that this "pre-certification audit" of confidential expenditure vouchers should be followed by, "commercial type audit (selective sampling)" by the Audit Office in substitution for the exhaustive individual voucher review then being conducted. [redacted] suggested that time savings by the Audit Office under the suggested procedure would not only provide for more current audit reports, but would also provide time for audit evaluation of accounting procedures and other facets of internal control and financial management both internally and in proprietary and subsidy projects. He also recommended greater utilization of witting or unwitting public accounting firms to perform audits of commercial projects, [redacted]

[redacted] These recommendations of [redacted] were adopted in essence to form the basis of a new Agency audit policy. [redacted] selected to implement the recommended pro-

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gram himself, was appointed as Auditor-in-Chief on 18 January 1952.\*<sup>17/</sup> The appointing notices provided that the Auditor-in-Chief would be responsible to the Director through the DDA for the audit (exclusive of internal audit)\*\* of all finance, fiscal, and property matters not under the General Accounting Office procedures, and for assuring that appropriate current audits were made.<sup>18/</sup> The notice stipulated that security would be a basic consideration in all audit actions and recommendations. The CIA Auditor was subordinated to the Auditor-in-Chief,

[redacted]  
[redacted] It may be presumed that the appointment of this man of commanding physical appearance, a pleasant yet forceful personality, and impeccable character as Auditor-in-Chief was motivated in part by the Agency's desire to assure Congress regarding the control of confidential funds.

\*\*Internal audit as understood in this notice was the routine examination of transactions and records by certifying officers or other employees within the various Agency components to be subsequently audited by the Audit Office.

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but in actual practice the routine of Headquarters audits was not interrupted at this time. [redacted]

[redacted] as CIA Auditor, remained in charge of the Audit Office, and [redacted] maintaining an office remote from the Audit Office, served on the DDA staff and formulated future audit policy, particularly as regarded the feasibility of decentralizing post-audit to the foreign field. At this time, as noted previously, the Audit Office was staffed with a total of [redacted] professional and clerical employees. These were informally grouped into a fiscal audit section and a property audit section. This grouping was more the result of the physical location of the property group near the Logistics Office than of any deliberate attempt at organization. Supervision of all audits and review of all reports was centralized in the CIA Auditor. In order to expedite the completion of audits and the release of audit reports, audits of funds and property were assigned by individual financial and property accounts rather than in total as was

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previously the case.

The lack of sophistication in Agency accounting methods and controls at this time was exemplified by the findings of an audit of the Special Stock Account - Procurement and Supply Office, for the period February 1951 through May 1952. The report of audit, released 14 July 1952,<sup>19/</sup> noted that although [redacted] had been advanced during the period to a special procurement agent, no books of account were maintained to reflect the disposition of this sum by either the agent or the Agency. The auditor was therefore obliged to recreate a record of transactions and accountability from the bank statements, cancelled checks, check stubs, letters of credit, bank debit advices, invoices, and delivery documents. As a result of this audit, arrangements were made for the agent to provide the Agency with papers and documents necessary to permit the maintenance of a current record of accountability and disposition of funds advanced.

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### III. The Expanding Scope of Audit, 1952-59

Consistent with [redacted] concept of the role of audit in the Agency, certain audit functions previously performed by the Finance Division (formerly the Confidential Funds Branch) were assigned to the Audit Office or directly to the office of the Auditor-in-Chief. The first of these was the audit of proprietary projects, which was transferred to the Audit Office in September 1952.<sup>20/</sup> The audit program for these projects as inherited from the Finance Division or developed by the Audit Office required annual site audits of each project by staff auditors, or by commercial audit firms employed to perform site audits of projects which could not securely be visited by staff auditors, or which required certified public accountants' reports for cover purposes. In this latter regard, relations were developed with major public accounting firms with international repre-

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sentation to permit Agency-directed and instructed audits by cleared auditors who could be made witting of Agency interest or not as circumstances warranted.<sup>21/</sup> These firms performed audits of approximately 5 percent of all proprietary companies, but the Agency's investment in these companies was substantial. The development of commercial audit programs for proprietary projects, the performance of commercial audits, and the instruction of certified public accountants required the employment or development of highly qualified staff auditors. These auditors were recruited primarily from the General Accounting Office and, after training in intelligence disciplines, formed the nucleus of the expanding audit force. Reports of audits of proprietary projects were often the best information Agency management had on the internal finances and business activities of these projects. Audit findings were usually routine in nature and dealt primarily with protection of Agency investment, internal controls, accounting procedures, and

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financial reporting. These were used in the formulation of future administrative plans for project funding, financial control, and business management. Some instances of misuse or conversion of Agency investment were reported. These were usually attributable to character weaknesses of corporate hire managers or employees.

A second responsibility transferred from the Finance Division was that of site audit of Agency field station accounts. Prior to late 1952, confidential funds officers at major stations and designated custodians at smaller stations submitted monthly financial accountings to Headquarters for audit and certification. A desk audit of selected station accountings and supporting documentation was made subsequently by the Audit Office.22/

Site audits in the field, although long recognized as necessary and desirable by management, were not the practice except in connection with occasional field visits by executives of the Finance Division.23/ The need for initiation of

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independent audits at field stations, which had been under consideration since 1947, was dramatically emphasized through observations made as a result of a desk audit of a field station for the period ended 30 June 1949. The report of this audit, issued 2 August 1950,<sup>24/</sup> disclosed that lack of accounting records and poor supervision and control had resulted in extensive black market transactions with Agency supplies to the personal gain of a Station employee, in the accumulation of unrecorded cash funds at the Station which were used for unreported operational entertainment and other purposes, in personal loans from unrecorded funds and in unauthorized use of Agency military purchasing privileges.

The Director of Central Intelligence reacted to this report with appropriate disciplinary action toward those responsible, and with the observation that audits of field stations must be continued.<sup>25/</sup> The Executive for Inspection and Security noted that this case indicated that the protection of

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the Agency and the Director demanded future administrative inspections in the field by inspection and audit facilities answerable only to the Director of Central Intelligence.<sup>26/</sup> Concurrent with [redacted]  
[redacted] subsequent study of the feasibility of decentralized audit of field activities, the Finance Division concluded that certification of field accounts would also be best accomplished by assignment of senior finance officers to major field stations. Both concepts were implemented simultaneously in October 1952 by the assignment of authorized certifying officers [redacted]

[redacted] This unit

consisted of three auditors who had been transferred from the Audit Office to the T/O of the [redacted] Division. The unit was initially under the direction of [redacted]

In order to defend the technical independence of the audit group from local influence, a Memo-

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randum of Understanding, dated 19 March 1953, provided that auditors would be subject to the administrative supervision of the Senior Representative,

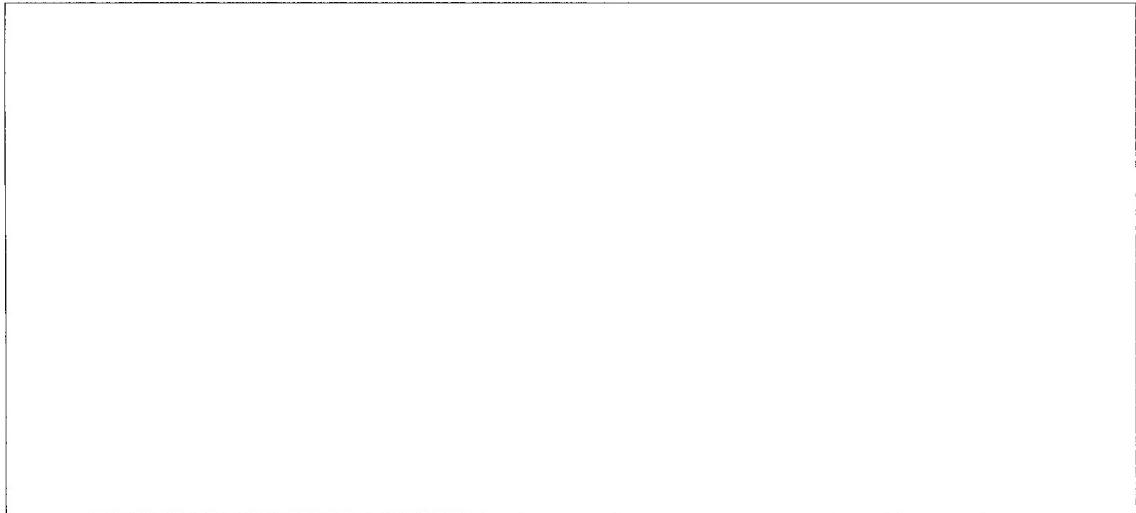
[redacted] but would receive technical direction from the Auditor-in-Chief. Direct and privileged communication of audit matters between field and Headquarters was established using the indicator [redacted]

[redacted] Allotments of funds for staff salaries, housing, travel, and other costs of support were transferred from the Audit Office at Headquarters to [redacted] Division.

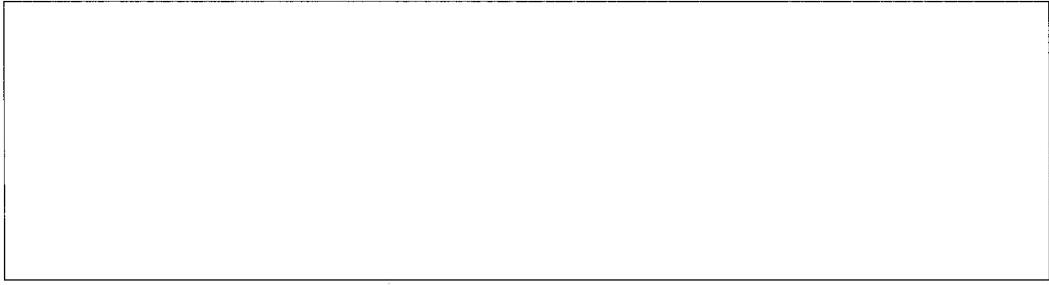
The foregoing pattern was repeated in May

1953, with the establishment of an audit unit in [redacted]

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This deployment of field auditors continued  
for several years, with the exception of the [redacted]

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The field audit program as initially imple-  
mented by [redacted] required a site audit at  
four-month intervals of all major field stations  
to which certifying officers were assigned (Class A  
stations) and at annual intervals of small stations  
which continued to forward monthly financial reports  
to Headquarters for certification (Class B stations).  
Audits consisted of physical verification of cash

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and property inventories, examination of advance accounts for excessive delinquencies, and of broad reviews of vouchered transactions for authorities, approvals, certifications, documentation, accounting disposition, and accuracy. Internal controls and other protective procedures were tested to determine appliance and effectiveness.

Reports of audits were prepared in the field for chiefs of stations, and copies were forwarded to Headquarters for dissemination to concerned Agency officials. Field audit reports of this period emphasized deviations from regulatory requirements and good accounting practice with regard to financial controls over advances and expenditures of confidential funds, accounting records and reports, and cash and property custodial practices. Such findings reflected the relatively autonomous nature of field station management at that time, which often tended to subordinate financial and logistical management to operational and administrative expediency, or worse, to ignore it completely.

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In some instances audit findings and recommendations were disputed by local officials as being impractical or unnecessary under existing conditions, but normally reports were well received and corrective action initiated during the visit of the auditors.

Headquarters management reacted to these reports with specific instructions for compliance with existing regulations, or in more general areas, with more detailed procedural guidance in handbook or field notice form. The audit [redacted] for the period ending 30 September 1955 was representative of field station audits of this period. The audit report<sup>29/</sup> contained thirty summary recommendations for the correction of matters such as delinquent advance accounts [redacted] noncompliance with subsidy project administrative plans, advances and expenditures of funds without management approval, ineffective controls over cash and supplies, inadequate documentation of financial transactions, failure to dispose of surplus vehicles which had been replaced, and other

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less significant procedural or record deficiencies. The Station response to this report<sup>30/</sup> was defensive in tone and stressed the impracticality of many of the audit recommendations. Headquarters reinforced the auditors' recommendations with instructions for compliance with existing regulatory requirements and acknowledgement of the validity of procedural changes recommended by the auditors which were based on sound accounting principles although not formally required at the time by Agency regulations.<sup>31/</sup> The Headquarters position on this and other audit reports at the time established the credentials of the Audit Staff and provided a base of confidence for successive audits.

By early 1957, remarkable improvement in the field management of funds and property became apparent. Repetitive audits at field stations continued to review local management procedures in terms of increasingly sophisticated criteria provided by Headquarters, and the nature and number of deficiencies cited in audit reports waxed and

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waned, dependent on the attitudes and capabilities of incumbent chiefs of stations and support and finance officers. Field audit reports became useful to Headquarters evaluators as informal indicators of the competency of field managers, and partially as a result of audit findings, training programs were initiated to prepare employees designated as custodians of funds or property for these duties. Such training programs were especially valuable for staff secretaries assigned to small field stations where they functioned as general support and communications officers as well as secretaries to chiefs of station. Improvement through this program was especially evident in stations in the [redacted].

Further improvement in support management at these stations resulted from the establishment by the Office of the Comptroller of senior finance officers at large stations in these areas to certify the accountings of small stations and to provide technical supervision and guidance to custodians

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of funds. These supervisory centers were designated as [redacted] stations.

The primary difficulties encountered in the establishment of the field audit program were the recruitment of Headquarters auditors for field assignments and the maintenance of the four-month audit cycle. The first of these problems was temporarily overcome by the recruitment of auditors specifically for field assignments. In later years, the enthusiasm generated by returnees served to make field assignments desirable to all auditors and competition was lively for each vacancy. The second problem proved more difficult. After the initial period of intense audit which resulted in general improvements of accounting practices and financial management, [redacted] relaxed the Class A station audit cycle to six months and established the policy that field auditors would not be absent from their home station more than six months in each calendar year.

These efforts were not completely effective,

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however, as some senior auditors continued the detailed voucher audit technique in which they had been trained at Headquarters and in previous employment. Audits conducted in this manner could not be completed in the time allocated, and as in Headquarters, reports were delayed and annual audit programs were not completed. This problem was to exist for several years, until resolved through firm direction from Headquarters and by the gradual replacement of older auditors through retirement and attrition. In fairness to these auditors, it should be noted that the detailed audit method was applied with the highest professional integrity in accordance with previous training.

The audit policy developed by [redacted] together with the mission, authorities, and responsibilities of the Auditor-in-Chief and the chiefs of field audit units, was formalized in August 1954 in CIA regulations. This policy, briefly stated, was to provide audit facilities and services equivalent to those now available to other departments and

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agencies of the government to ensure the highest possible protection to government assets consistent with security limitations necessitated by the nature of Agency operations.<sup>32/</sup>

By October 1954 the expanded work load and scope of audit required reorganization of the Office of the Auditor-in-Chief. As previously noted, the Audit Office had been separate in organization from the Auditor-in-Chief, and functionally not related to the field audit program (see Figure 1). The organization of the Audit Office was monolithic in structure. Auditors were assigned to either the Field Branch or the Property Branch, but all Headquarters work assignments were from the Auditor (Chief, Audit Office).

The new organizational structure combined all audit groups as the Audit Staff\* on 16 February 1955, shortly after the DDA became the Deputy Director for Support. The position of Auditor-in-Chief was redesignated as Chief, Audit Staff. The

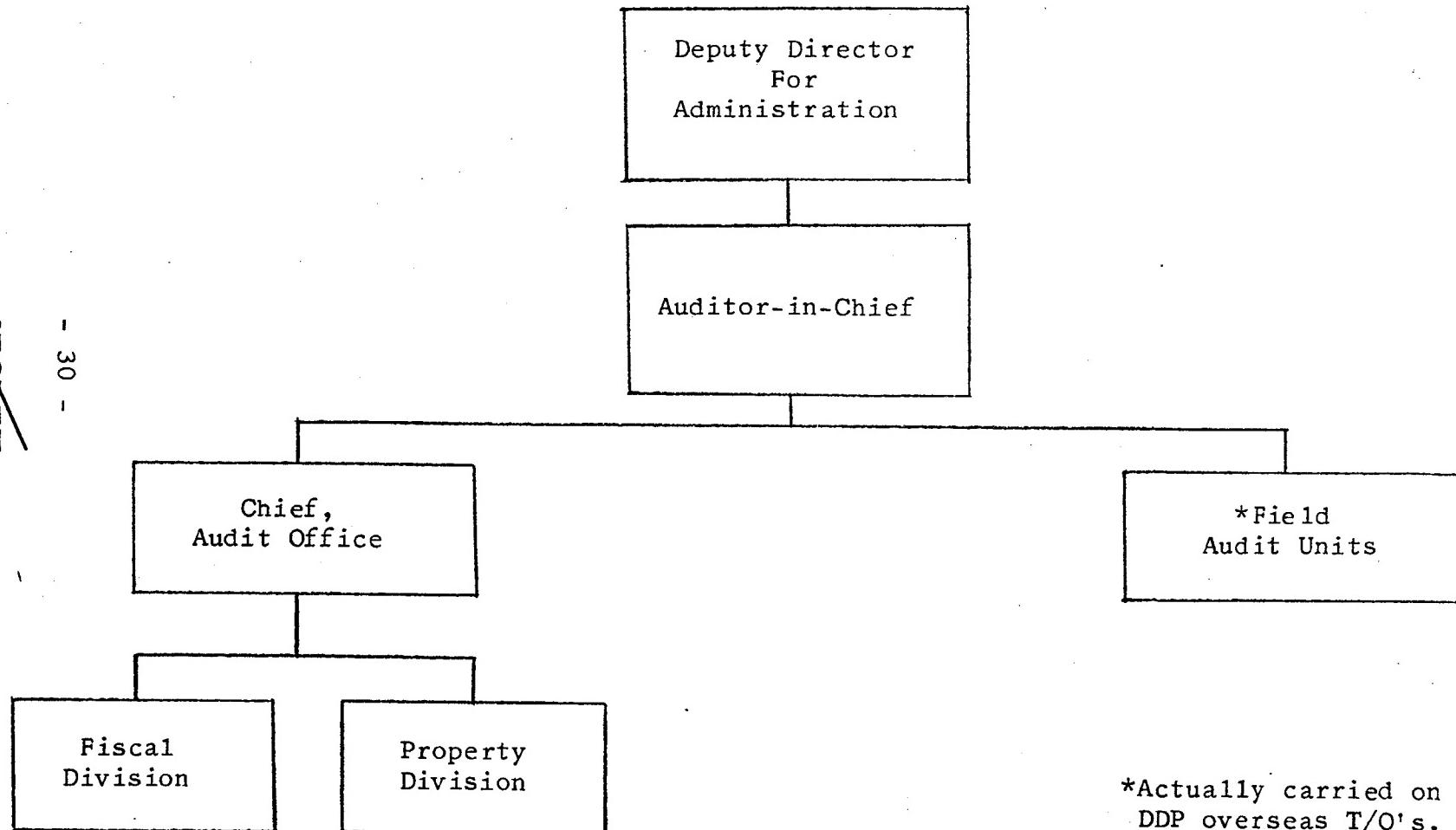
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\*See Figure 2, page 31.

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Office of the Auditor-in-Chief  
30 June 1953

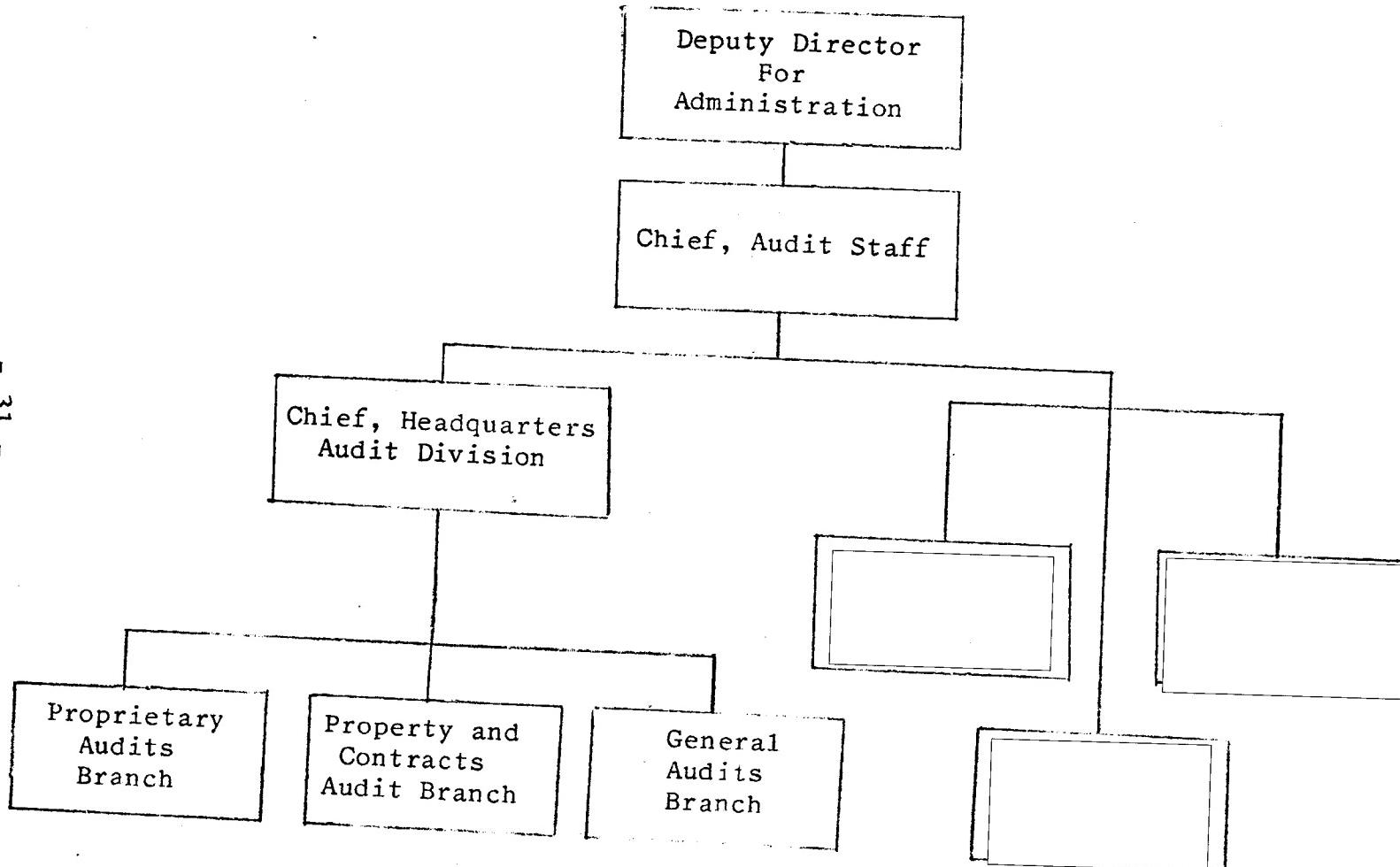
Figure 1



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Audit Staff Organization  
31 December 1955

Figure 2



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The Audit Office, with [ ] as Chief, was redesignated as the Headquarters Audit Division, which consisted of a General Audits Branch, a Proprietary Audits Branch, and a Property and Contracts Audit Branch.<sup>33/</sup> These branches were initially supervised by [ ] and [ ] respectively. The field audit units remained under the direction of [ ].

On 30 November 1955, in response to a recommendation by the Inspector General,<sup>34/</sup> all field auditor positions were transferred from the T/O of the Deputy Director for Plans to the T/O of the Audit Staff.<sup>35/</sup> These organizational changes and consolidations resulted in increased independence of the audit function and permitted more flexibility in Staff personnel management. As of 31 December 1955, through the efforts of [ ] the Audit Staff had an authorized strength of [ ] professional and clerical employees deployed in three Headquarters branches and three field units. This organizational structure continued through 1960 --

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with minor changes in January 1957, when the position of Assistant Chief, Audit Staff was established,<sup>36/</sup> and in February 1959 when all field units were grouped into the Field Audit Division under the direction of the Assistant Chief, Audit Staff.<sup>37/</sup>

The years 1955 through 1958 were spent in the collective accumulation of experience in the unique field of audit of clandestine operations. In this latter regard, fundamental differences were found to exist between the conduct of audits and the qualifications of auditors in the conventional government service or in public accounting and the conduct of audits and qualifications of auditors in the Agency. Primary among the differences was the paramount need for operational security. This was the basis for the existence of the confidential funds legislation, and a consideration in every audit. This requirement manifested itself in various ways. The use of cash rather than checks for even the most routine administrative expense

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served to prevent association of the transactions with the Agency or the government, but also required that the audit be much more intense and that more emphasis be placed on internal safeguards and procedural controls.

Site audits of clandestine activities were complicated by the need for auditors to maintain light cover compatible usually with the installation or activity under audit. This deprived Agency auditors of the interdepartmental liaison available to other government auditors in foreign administrative environments. Journeyman auditors were obliged to recognize operational priorities and the degree of protection required for operational relationships in order to determine the documentation necessary or available to substantiate cash disbursements. Auditors were also required to be broadly experienced in all phases of governmental and commercial audit. The limited strength of the staff did not permit development of specialists as was the procedure in other government agencies.

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Thus the same senior auditor might be assigned to an audit of a [redacted] on one audit, an [redacted] on the next, a [redacted]  
[redacted] on the next, a [redacted] project on the next, and so on. Auditors were also required to travel alone in remote areas of the world without a ready source of guidance or supervision.

Accounts and activities audited were likely in some cases to be deliberately distorted in order to disguise sources and applications of funds. In such cases, auditors were obliged to identify and eliminate falsified transactions in order to evaluate such transactions and to prepare covert financial reports for the information of Agency management. Auditors were sometimes required to operate in relatively dangerous circumstances, not the least of which were frequent flights on unscheduled military or clandestine aircraft, or unreliable air carriers of underdeveloped nations.

The expertise necessary for the conduct of

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audits as described above was developed through on-the-job experience and through formal Office of Training programs for administrative and operational support. External professional training was also encouraged and current developments in the auditing profession were monitored through membership in professional organizations and subscriptions to professional journals.

One deficiency cited by the Inspector General as a result of his survey in 1955 was the quality of written reports of audit and the scarcity of competent reporters on the staff.<sup>38/</sup> A general fault of audit reports of that time was a tendency to criticize superficial deficiencies without delving into and reporting fundamental causes. This weakness stemmed partially from a reluctance of audit management to expand audit beyond the familiar and relatively safe environment of financial and logistical accounting records to the unexplored areas of operational offices. Thus an audit report might expound at length on deficiencies in accounting reports received by the

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Finance Office with implied criticism of financial management when the major cause of the accounting deficiency might have been found and correctly evaluated in the responsible operating element. Further experience of both auditors and supervisors, coupled with constructive criticism by recipients of such reports, led to expanded audit coverage and more accurate reporting.

[Redacted]  
[Redacted]  
respectively, contributed greatly to the reputation and credibility of audit during this period by insistence on accuracy of content and clarity of presentation of audit reports.

A major problem encountered during the early days of the Audit Staff which persisted through the 1950's was the reluctance of operations officers to accept audit of funds and property in their custody, and to provide auditors with even the most superficial information regarding operations under their direction. This attitude was attributable to

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a number of causes, among which was a legitimate doubt regarding the need for auditors to know details regarding operations. Some case officers also presumed that audit of their accounts reflected doubts of their personal integrity. Operational personnel during these years were not necessarily aware of their role as ultimate financial managers of operations, and in some cases they assumed that regulations and requirements regarding support assets were directed exclusively to support personnel. This problem was gradually overcome through training which was programmed to orient all Organization personnel regarding the functions and responsibilities of other components and through personal contact and persuasion by auditors. Agency regulations were amended to provide a formal recourse and executive review of activities encountered which were locally determined to be too sensitive for audit. In all cases submitted, determination was made to permit audit by cleared auditors. As a result of the broad

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representation of audit at Headquarters and in the field, official and personal relationships were formed between auditors and administrative and operational personnel which persisted in later years and greatly enhanced audit access and influence in all areas.

As previously related, [redacted] concept of the Audit Staff function was that of external audit\* in lieu of the GAO audit provided

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\*External audit refers to examination of financial activities of an organization by a firm or auditing body from outside the organization. In the US Government responsibility for such audit is assigned by law to the General Accounting Office. [redacted] initial concept of the role of the Audit Office was limited in context to independent review of the records and transactions of the Office of the Comptroller. In this context the Audit Office function was one of an "outside" or external body, while the review of the same records and transactions by the Certifying Officers of the Office of the Comptroller was construed as "inside" or internal audit. This concept was accurate as long as Audit Office review was limited in scope to the Office of the Comptroller, but became less valid when the scope of audit was expanded to include procedures and controls exercised by other Agency components. At this point the Audit Staff became an internal (Agency) audit function as opposed to an external (GAO) audit.

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normal government agencies.<sup>39/</sup> The emergence during the late 1950's of internal audit as a distinct sub-discipline within the auditing profession provided a technical frame of reference which began to be recognized as a closer definition of the role of audit in the Agency. Internal audit was described in 1957 by the Institute of Internal Auditors as

...an independent appraisal activity within an organization for the review of accounting, financial, and other operations as a basis for service to management. It is a managerial control which functions by measuring and evaluating the effectiveness of other controls.<sup>40/</sup>

Implementation of this management service by Audit Staff was begun under the direction of the Chief, Headquarters Audit Division, [redacted]  
[redacted] who sought to realign the audit of Agency accounts and expenditures of funds and property to conform with management responsibilities and authorities. With the assistance of [redacted] then Chief of the General Audits

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Branch, [redacted] arranged with the Chief of the Western Hemisphere Division of the Plans Directorate for an audit of the Division for the period ended 31 December 1958.

The audit was conducted in a manner similar to that of a Class A field station, with all personal and operational accounts charged to WH Division confirmed within the Division, and all expenditures and issues reviewed in context of Divisional budgetary authorities, project approvals, and other authorities. In actuality, the audit did not constitute a departure from audit processes previously applied, but merely changed the focus of audit. Thus, rather than to examine an account maintained by the Office of the Comptroller or the Logistics Office which reflected accountability of or expenditures by all Agency components, this audit segregated that part of the accounts which reflected only the activities of the WH Division. From the point of view of the Division, the major discernible difference was in the direction of the

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recommendations in the report of audit and the Division responsibility for corrective actions and reply to the report.

This report was presented to the Chief, WH Division on 27 March 1959 for corrective action except as audit exceptions required action by the Office of the Comptroller.<sup>41/</sup> The management oriented approach to audit proved a success and was well received by WH and higher Agency management and consequently audits of all organization components were conducted in this manner on an annual program.

A peripheral benefit which evolved from component audits was the exposure of auditors to the existing relationship between the mission and functions of components audited and the utilization of Agency resources in the performance of these functions. This new orientation provided the essence of an audit technique which, although not recognized by the Audit Staff at the time, would later be identified by the General Accounting Office

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as comprehensive audit.\*

The immediate result of the broadened audit perspective was apparent in simultaneous audits of financial and property activities of the Technical Services Staff (TSS) of the Plans Directorate. The reports of these audits, dated 31 July 1959 and 11 December 1959, respectively, indicated thorough review of financial programming for the research and development [redacted]

[redacted]

The financial report was highly critical of TSS budgetary procedures and questioned the legal authority of TSS to obligate funds of prior or lapsed fiscal years through means of contractual over-runs. This matter was referred to the DDS by the Office of the Comptroller<sup>42/</sup> and ultimately to

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\*See p. 55 below.

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the Office of General Counsel for resolution.<sup>43/</sup> Subsequent financial audits of TSS indicated that the deficiency had been corrected by adoption by TSS of more accurate budgetary programming methods. The property audit disclosed a number of deficiencies in property controls, procedures, and custodial facilities which had resulted in numerous unexplained shortages and overages of equipment and supplies. The report observed that most deficiencies were due to complexities of TSS operations and noted the willingness of TSS officers to cooperate in the resolution of these problem areas. Continued efforts by TSS to correct these problems were reflected in subsequent reports of audit.

A further indication of the growing confidence of Agency management in the Audit Staff was the assignment of auditors with necessary operational clearances to audit sensitive components, projects, and activities previously exempted from review under DCI waivers. Thus highly classified activities of the Development Projects Division, the

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Special Projects Division of the Counter Intelligence Staff, and other DDP divisions and staffs were subject to the same degree of financial inspection as was applied to other less sensitive components.

Among these activities, perhaps the most challenging were the projects associated with the development of the U-2 reconnaissance aircraft by the Development Projects Division (DPD)\* of the Plans Directorate. The extremely sensitive operations of this component were segregated from the normal organization of the Agency and thus exempted from the routine of normal procedures, controls, and reviews by the Office of the Comptroller and the Office of Logistics, although qualified personnel from these components were detailed to perform the administrative work of the Division. Auditors with appropriate clearances were assigned to review the

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\*Later combined with other technical components to become the Directorate for Research, and still later, the Directorate for Science and Technology.

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financial and logistical activities and operational phases of these projects.

Audits of these activities emphasized the negotiation and administration of commercial contracts for the research and development of the technical equipment and supplies used in the performance of these activities, personal service contacts with professional or technical personnel for the operation of project equipment, and the conformance of Division staff managers with applicable Agency regulations and directives governing the control and use of Agency or other government agency funds and equipment. Annual reports of audits of DPD dating from 31 January 1957 reflected the competent management and efficient operation of these projects. Auditors conducting these continuing audits gained invaluable experience in contract auditing techniques and in the procurement and utilization of sophisticated technical collection media.

By late 1959 all field installations and

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activities were audited at least annually by field-based auditors except those in the Western Hemisphere area, which were audited by auditors on temporary duty from Headquarters.<sup>44/</sup> [redacted]

[redacted] had received official concurrences from the establishment of a field audit unit [redacted]

[redacted] in August 1957, but difficulties in staffing the unit caused delay.<sup>45/</sup> The unit was finally established in January 1960 with the assignment of two auditors under direction of [redacted]

The initial experiences of auditors assigned [redacted] proved again the value to

Agency management of field audit units. The first reports issued by this unit indicated that field administration of Agency funds and property in the Western Hemisphere area was not equivalent to that applied in other field areas. The report of audit [redacted] for the year ended

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\*This unit was later increased to three auditors.

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30 November 1960<sup>46/</sup> contained the observation that significant weaknesses in station internal control procedures were noted, and commented on twenty-four specific deficiencies leading to this general observation. As in other field areas, these deficiencies related to delinquent advance accounts, inadequate cash controls, insufficient documentation of financial transactions, insufficient supervision and control of subordinate unit accounts, and other procedural and control shortcomings. The station reply<sup>47/</sup> reported that corrective action had been completed or was in process regarding most reported deficiencies. The reply also observed that the auditors had erred in reporting two items, and submitted extenuating circumstances in justification of a third deficiency reported.

Subsequent audits of this station noted marked improvement in all areas. Audits of smaller stations indicated similar patterns. The report

[redacted] dated 18 June 1960<sup>48/</sup> reported

nineteen deficiencies in local accounts, controls,

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and procedures. The following audit, reported on 30 June 1961,<sup>49/</sup> commented on only three minor deficiencies. This latter report commended station personnel for their efforts and accomplishments during the audit period. A broader effect of the presence of the audit unit [redacted] was the increased interest in and supervision of support activities by WH Division at Headquarters which was presumably generated by frequent reports of audit.

Shortly after the establishment [redacted]  
[redacted] the chief of the unit was required to participate in a series of Headquarters-coordinated audits of activities mounted to counteract the emerging threat from the Communist government of Cuba. Perhaps in recognition of the value of audit as a device for monitoring support management, Agency management requested that an auditor be assigned to these activities from inception. A senior auditor, [redacted] was given this task of auditing Headquarters and domestic field

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phases of these operations and of coordinating audits of foreign field activities. [redacted]

initial report covering the support activities at the forward operating base and communications facility of [redacted] was released 30 November 1960<sup>50/</sup> and covered the period from its inception in May 1960 through 10 October 1960. The report observed that although support and operations personnel had discharged their custodial and control responsibilities with diligence and vigor, numerous deficiencies in internal control techniques and documentation of financial and property transactions had developed. The report attributed these to the pressures and distractions inherent in activities undertaken in crisis situations.

Thirty-four specific deficiencies were cited in custody and control of cash and administration and control of travel and per diem, property, advances, and operational expenditures.

Administrative actions recommended for correction of these deficiencies included estab-

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lishment of policy with regard to provision of living quarters for employees; reduction of per diem rates when quarters were provided without cost to employees on temporary duty; establishment of controls over assignment and use of official vehicles; designation of a control authority to authorize travel and approve travel costs; and limitation of access to cash imprest funds to custodians.

A second audit report of these activities for the period 11 October 1960 to 31 May 1961 stated:

During the audit period operational activity at (the site) reached its apex and then began a rather rapid decline. Financial and property transactions were both voluminous and complex, and employees were under great stress. Since it was thought originally that the project was to be very short in duration, little effort was made to establish and maintain more than the most fundamental of controls. When the project did not succeed in its original objective, however, it was decided to convert it to a more permanent status. In conducting our audit, therefore, we minimized

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deficiencies in procedures and controls relating to the past, and emphasized improvements and refinements which should be made to bring them up to the standards normally expected of permanent field stations and bases.<sup>51/</sup>

This report then listed 20 summary recommendations for the accomplishment of this stated objective. These included recommendations for formalization of field agents' relationships with the Agency by the preparation of Memoranda of Oral Agreement setting forth salary rates and other rights and benefits due agents; for strengthening controls over safehouse utilization; for evaluation and formalization of motor vehicle requirements; and for more effective records and procedures to control use of equipment and supplies.

The next successive audit report for the period ending 26 April 1962 observed:

Although this report reflects numerous matters requiring attention by field and Headquarters, overall we feel that management and administration of the Station have improved significantly since our last audit.<sup>52/</sup>

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Such audits and reports were continued until the  
termination of this activity on 15 November 1968.

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~~SECRET~~IV. Audit of Voucherized Funds, 1959-60

While the Audit Staff was evolving through audit of confidential funds and property, auditors from the General Accounting Office on detail to the Agency were performing voucher audits of overt or "voucherized fund" expenditures. Segregation of the voucherized and confidential expenditures was provided through the Agency financial management and accounting system in effect until 1966. Under this system, the Fiscal Division of the Office of the Comptroller maintained conventional governmental accounting records of all funds appropriated for Agency use.

Disbursements of appropriated funds under certification by the Director of Central Intelligence as provided in Public Law 110 were transferred through a system of reciprocal accounts to the confidential accounting records of the Finance Division. Other expenditures and advances of

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appropriated funds were obligated, vouchered, certified, and disbursed by Fiscal Division in accordance with normal governmental procedures. These transactions, primarily for overt payrolls, procurement of services, supplies, and equipment, and domestic TDY travel, were those audited by GAO auditors. The postwar emphasis on efficiency in governmental management and the broadening scope of internal audit as a management reporting device led to the development in 1949 of a "comprehensive" audit program by the General Accounting Office. The stated purpose of this program was

to determine how well the Agency or activity under audit has discharged its financial responsibilities. Financial responsibilities in this case are construed as including the expenditure of funds and the utilization of property and personnel in the furtherance only of authorized programs or activities in an effective, efficient, and economical manner.<sup>53</sup>

In June 1959, as a result of congressional inquiries, such an expanded audit was proposed by

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the Comptroller General for the Agency to supplement the voucher audit then in effect.<sup>54/</sup> The audit, as proposed, was to review overall organization and all internal policies, practices, and procedures. All vouchered transactions were to be reviewed, and to the extent necessary to test financial controls, confidential fund transactions were to be examined as well. Allen Dulles the Director of Central Intelligence, in notifying the President of the United States of the proposed audit, welcomed the audit of vouchered funds but expressed reservations with regard to the audit of confidential funds.<sup>55/</sup>

High-level discussions continued with GAO from May 1959 through January 1960 throughout which GAO sought to expand its scope to permit comprehensive audit, and the Agency steadfastly maintained the position that, while vouchered funds transactions and all non-sensitive Agency functions were available to GAO auditors, the clandestine services and the confidential funds

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authority must remain inviolate. The Agency's position during these meetings was that the intent of Congress as expressed in the Central Intelligence Act of 1949 was to exempt the confidential funds of the Agency from review by the General Accounting Office. This position, based on the provision of the Act which stated

The sums made available to the Agency may be expended without regard to the provisions of law and regulations relating to the expenditure of government funds; and for objects of a confidential, extraordinary, or emergency nature, such expenditures to be accounted for solely on the certificate of the Director and every such certificate shall be deemed a sufficient voucher for the amount therein certified.<sup>56/</sup>

was communicated by Dulles to the Comptroller General of the United States with the Director's invitation to continue exploration of means by which the GAO audit could be broadened consistent with security requirements.<sup>57/</sup>

In January 1960, GAO agreed to accept these legal limitations and to attempt audit without

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access to sensitive information.<sup>58/</sup> This audit continued through December 1960 and an interim report was prepared of the findings. In May 1961, on the basis of experience gained during this audit review, the Comptroller General notified the Chairman of the House Armed Forces Committee that broad audit of the Agency was not possible in view of the limitations imposed for reasons of security. It was agreed, however, that the limited program of voucher review should be continued. The representation from GAO continued until June 1962, when even the token presence was removed. The Comptroller General noted, in discontinuing the audits,

we do not have sufficient access to effectively accomplish any worthwhile audit objectives at CIA on a continuing basis.<sup>59/</sup>

With the total withdrawal of GAO from the Agency, the Audit Staff assumed final audit responsibility for all Agency activities and funds, both vouchered and confidential. This Audit Staff responsibility is unique in the United States Government.

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V. Comprehensive Audit of Agency Activities, 1960-67

[redacted] retired in May 1960 at the age of [redacted] after nearly a decade of Agency service. He left behind an established world-wide organization of trained and experienced professionals routinely conducting audits of Agency activities as he had recommended in 1951. In his final report to the Director, [redacted] expressed his belief that the audits made and reports thereon had been of material assistance to Agency management in carrying out its function.<sup>60/</sup>

[redacted] was replaced in September 1960 by [redacted] an Agency-developed executive who was formerly [redacted] of the Office of the Comptroller and, more recently, Comptroller of the [redacted] Station. [redacted] brought to the Audit Staff an accumulation of experience in the management of financial support of clandestine operations, and an intimate knowledge of the technology involved

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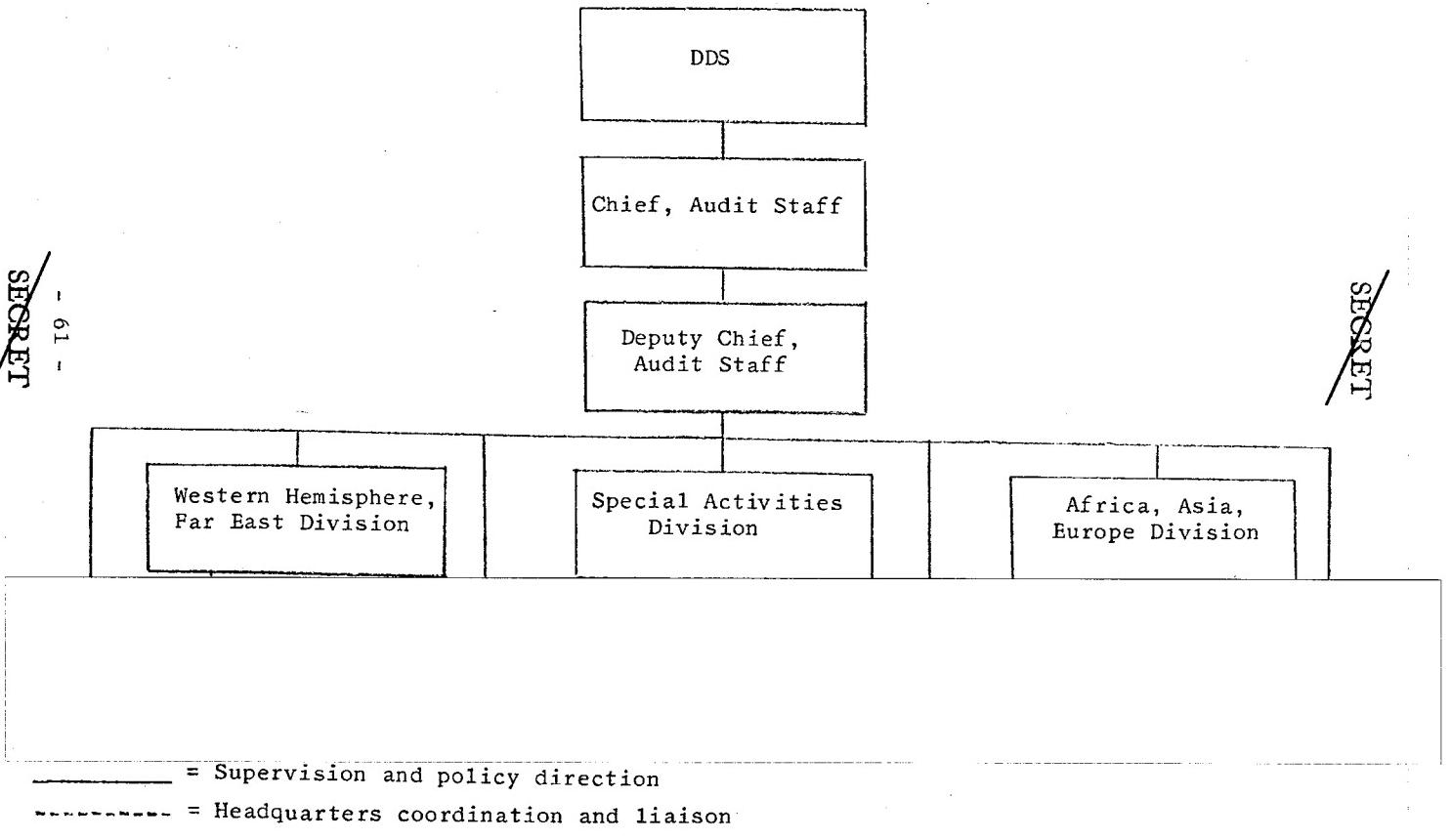
in such support. He endorsed the internal audit role of the Audit Staff and encouraged the development of a comprehensive audit program to the extent permitted by the clandestine nature of Agency operations.

In order to enhance the comprehensive approach to audit as well as to end over-specialization and provide more flexibility in Staff utilization, [redacted] reorganized the Audit Staff along lines of organizational authorities and responsibilities.<sup>61/</sup> The new Staff organization, effective in June 1961, included two geographical divisions which permitted alignment of audit responsibilities along the geographical command channels of the Agency and also provided for coordination of reports and other submissions of the Audit Staff field units in these operational areas (see Figure 3). A third division was formed to audit/special activities of the Agency which did not conform with geographical alignment. These included international world-wide organizations and [redacted] activities under official

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Audit Staff Organization Chart  
30 June 1961

Figure 3



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and commercial cover. As a part of this reorganization, [redacted] successfully proposed an overall upgrading of Audit Staff positions to equate auditors' grades with those of support personnel of comparable stature. [redacted] also prepared and distributed a "Handbook for Auditors" which set forth audit policies and standards for direction and guidance of Staff personnel.<sup>62/</sup>

A number of steps were taken to improve the quality and increase the impact of audit reports.<sup>63/</sup> The report format was redesigned [redacted] to provide top management with a concise summary of audit findings and recommendations at the beginning of each report with references to subsequent paragraphs containing the details of the findings. This permitted Agency executives to scan the reports, reading only those detailed comments which appeared to require action by them. Audit findings and recommendations were arranged in order of importance, and minor matters such as clerical or accounting errors which could not be corrected during the

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audit were omitted from reports and conveyed to lower management levels by means of separate memoranda. Audit reports were disseminated under cover sheets which explained the scope and objectives of the audit (see Figure 4). In many cases audit findings which might tend to sensationalize audit reports, such as cash shortages, ineptness of management, or specific instances of misfeasance investigated by Audit Staff, were reported in "Eyes Only" memoranda if at Headquarters, or in RYBAT dispatches from the field.

Through elimination of insignificant or sensational matters from reports a level of comparison was discernible against which management could evaluate the performance of individual installations or activities. In connection with these revised reporting procedures, the entire auditing-reporting-management reaction cycle was formalized. Audit findings, developed through professional application of established criteria for good accounting control and financial and

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Figure 4

# AUDIT STAFF

# REPORT OF AUDIT

This report presents the findings developed from an audit undertaken pursuant to Audit Staff responsibilities and authorities set forth in organization regulations. Unless otherwise indicated in the report, the audit included review and appraisal of internal controls and procedures and such other audit processes, test checks and verification of accounts, assets and transactions as were considered appropriate and consistent with generally accepted audit standards in the circumstances.

The objectives of the audit were to determine for management whether

- (1) Adequate controls and procedures have been established and are being applied effectively to safeguard organization resources and assure that resources are used only for approved and legal purposes, and
- (2) Activities are being conducted economically, efficiently and in conformance with policy determinations and directives.

*For the period:*

*From* \_\_\_\_\_

*Through* \_\_\_\_\_

*Date* \_\_\_\_\_

*This report consists of \_\_\_\_\_ page(s).*

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logistical management, were reported through the media described above to the component audited or to that level of management which could effectively correct or justify deviations from these criteria. Copies of reports were routinely provided to the responsible Headquarters division, to the various support directorates with technical responsibility for matters discussed, to the Deputy Director responsible for the activity audited, and to the Executive Director through the Inspector General.

Clandestine Services Instructions were published which required replies to audit reports through the responsible division.<sup>64/</sup> Copies of replies were also provided to the Inspector General on request. These replies were required to indicate acceptance of audit recommendations or to present those mitigating circumstances which the component believed were sufficient to justify the reported deviations from normal requirements and procedures. It should be noted that the Audit Staff assumed no command authority and that components audited were

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not obliged to accept recommendations without question. The objective audit report, while presenting a full discussion of facts pertinent to a developed audit finding, could not formally recognize any local condition such as an emergency or wartime environment, rapid expansion, operational priorities, inadequate staff, or other factors which may have caused a temporal decline in management effectiveness, as warranting deviation from prescribed controls over custody and use of Agency resources.

If local management seriously believed that special circumstances precluded acceptance of the audit recommendations, the reply to the audit report would present the extenuating circumstances and request authority from higher management to continue the practice in question. Decisions by higher management to permit deviations from normal practices were noted by the Audit Staff, and future audits did not pursue the same matter so long as the extenuating conditions continued. In some

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instances where replies to audit reports accepted recommended changes, and subsequent audits disclosed that the practices in question were in fact continued, the same matter was reported again with the observation that the recommendation was continued from the previous report. In such cases, higher management often reinforced the audit recommendation with direct orders to comply with regulations governing the practice reported.

An example of the above process was available in successive audit reports of Saigon (Vietnam) Station with regard to property accounting procedures and controls. The audit report of 28 February 1963 noted:

Due to the inaccurate and incomplete condition of property records and the inadequate internal control over property, we were unable to verify the accuracy of records of property on hand or on loan nor sic to ascertain that property was issued in accordance with approved programs and plans. ... We recognize that Station activity has greatly increased over the past two years; however, major discrepancies in the areas noted above have existed

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during the past three annual<sup>17</sup>  
audits.<sup>65/</sup>

These introductory comments were followed by detailed comments to the effect that although accountability for supplies and equipment issued to Vietnam Station was dropped when these supplies were issued from depots [redacted]

and other stations at time of shipment, the fact remained that inventory assets valued at over

[redacted] were stored in warehouses [redacted]

[redacted] The report recommended that a review be conducted to determine whether the Type II financial property accounting system\* was adequate for

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\*Type II property accountability procedures, [redacted]  
[redacted] were for application at those stations and bases having a relatively small amount of property and were based on the principle that all non-expendable property was in use or in temporary storage awaiting issue. The Type I procedures, which the auditors believed would be more effective at Saigon, were described in [redacted] as applicable to large stations with a depot logistical function and where Class A financial reporting procedures were followed and where a logistics accountable officer was assigned. These criteria applied to Saigon at the time of the audit.

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the needs of Saigon Station. It was requested that the results of this review be provided to Headquarters.

The conditions cited in this report as well as the two preceding reports with regard to property controls were stressed by the Chief, Audit Staff in his memorandum transmitting the report through the DDP to the Chief, Far East Division.<sup>66/</sup> Copies of the report were also provided to the Director of Logistics and the Comptroller. The Station reply<sup>67/</sup> included the results of the recommended review and concluded that the only feasible and practical system of accountability at the time was Type II. Headquarters accepted this conclusion, and the next two annual audits, while critical of logistical accounting controls, did not again recommend changes in the basic accounting system. By 30 June 1965 the logistics control situation had become critical, and the audit report of that date noted:

The Type II system is simply not designed to handle such volume; in fact, it has been modified to a

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considerable extent already in an effort to control the logistics activity, but even with these modifications, we do not feel it is capable of coping with the situation. ... Therefore, we again recommend that consideration be given to converting from a Type II to a Type I system.<sup>68/</sup>

In the Station reply to this second recommendation,<sup>69/</sup> reference was made to Headquarters policy as provided in previous dispatches from FE Division which stated:

In our opinion the validity of the reasoning upon which Headquarters based its approval of Saigon's request for the establishment and implementation of a Type II accountability system still applies, and it is our considered opinion that a change to a Type I system would present a recordkeeping and financial accounting burden that would defeat Station's continuing efforts to reduce "paper work" and to facilitate the logistical support of its operations.<sup>70/</sup>

They also stated:

As we are all well aware, Saigon Station is operating under unusual circumstances and conditions. This is true logistically support-wise as well as operationally, and as

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Station and Headquarters are agreed,  
Agency policy and procedures for  
Type II FPA at Saigon Station need  
to be amended to allow Station the  
greatest degree of flexibility and  
to minimize manpower requirements  
and the workload necessary for  
maintenance of formal Type II FPA.  
... Approval has been given for  
these amendments and ... Saigon  
Station is authorized to deviate  
from normal Type II FPA procedures  
to the extent necessary... 71/

Under this policy direction, Saigon continued Type  
II FPA procedures through July 1966, at which time  
the audit report noted:

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[REDACTED]

The report went on to note that [REDACTED] stated that Type II FPA procedures were designed for use at stations with a relatively small amount of property, and that such system was not designed for the large and active operation conducted by Vietnam Station.

In transmittal, the Chief, Audit Staff FE Field Branch stated:

In my opinion, for reasons I have stated in the report, it is unrealistic for Vietnam Station to be continued under a Type II Financial Accountability System. Accordingly, notwithstanding Headquarters objection to such recommendation in the prior audit Report, I have, with Station concurrence, again recommended a change to the Type I system. If, after proper reconsideration, Headquarters again concludes that the Type II system is the proper one for Vietnam Station, we will yield to this judgment and refrain from surfacing the matter in the future.<sup>73</sup>

The Chief, Audit Staff in forwarding the report to Chief, FE Division noted that the report discussed again the inadequacy of the Type II system and

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indicated that use of the system not only resulted in less than satisfactory control over property but required more time and personnel than would the Type I system.<sup>74/</sup> Vietnam Station concurred strongly in the recommendation and noted that unless overruled the recommended system would be adopted with all reasonable speed. In reply

Headquarters noted

Your recommendation following the recent audit of your Station with respect to conversion from Type II to a Type I FPA system has been the subject of much discussion here at Headquarters and the purpose of this brief reply is not to give you a definitive answer of approval or disapproval at this time, but rather to indicate that there is some further homework that we wish to do in reviewing this problem before giving you a final answer.<sup>75/</sup>

Vietnam Station replied:

The judgment to recommend conversion to Type I FPA was not contingent upon the audit recommendation. However, its agreement would appear to lend weight to this decision.<sup>76/</sup>

By February 1967, Headquarters reached a decision and advised Saigon, "Vietnam designated Type I

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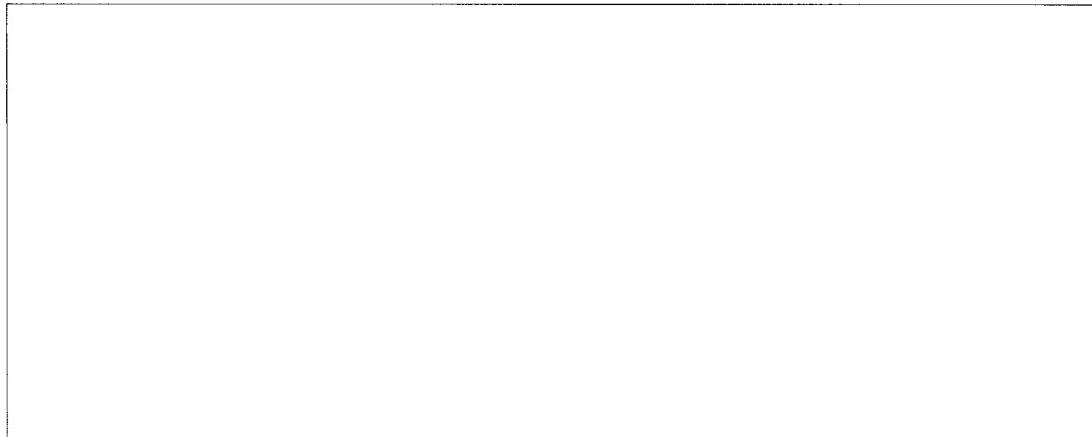
FPA installation effective 1 March 1967.<sup>77/</sup> The foregoing exemplifies in detail the mechanics of the audit reporting-management reaction cycle in one recommendation for one management change in a single station. This process is repeated in numerous cases of greater or lesser impact each year.

As noted previously, postwar emphasis on efficient management in government had led to a revision of the classic portrayal of internal audit. The auditor, who was previously caricaturized as a severe critic of narrow interest and influence, now was recognized as a reliable assessor and reporter of the effects of all phases of fiscal policy and management. The scope of audits, which had been limited to examination of accounting procedures, records and documents, was now expanded to the examination of every activity to determine for management whether adequate controls and procedures had been established and were being applied effectively to safeguard resources and to assure that resources were being used only for approved and

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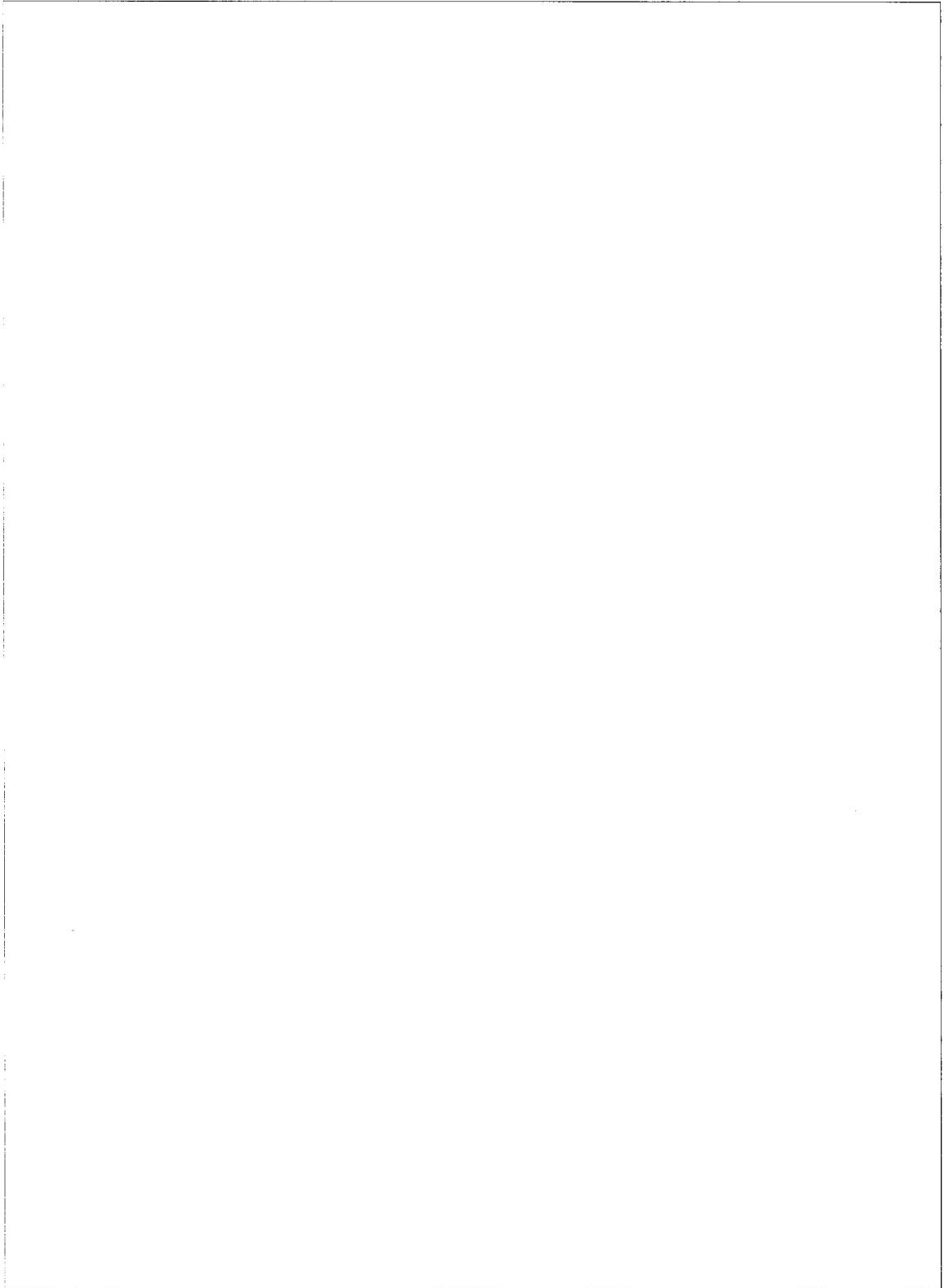
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legal activities, and whether these activities were being conducted economically, efficiently, and in conformance with policy determinations and directives. Throughout the period of [redacted] incumbency, these audit principles were applied gradually to the extent compatible with the restrictions imposed by the clandestine and classified nature of the Agency mission, and only insofar as effectiveness, efficiency, and economy of operations were measurable. Thus, while activities in support of clandestine activities or collection of foreign intelligence were audited within the scope of the comprehensive audit, no second judgment was made with regard to the need for or the effect of the activity supported.

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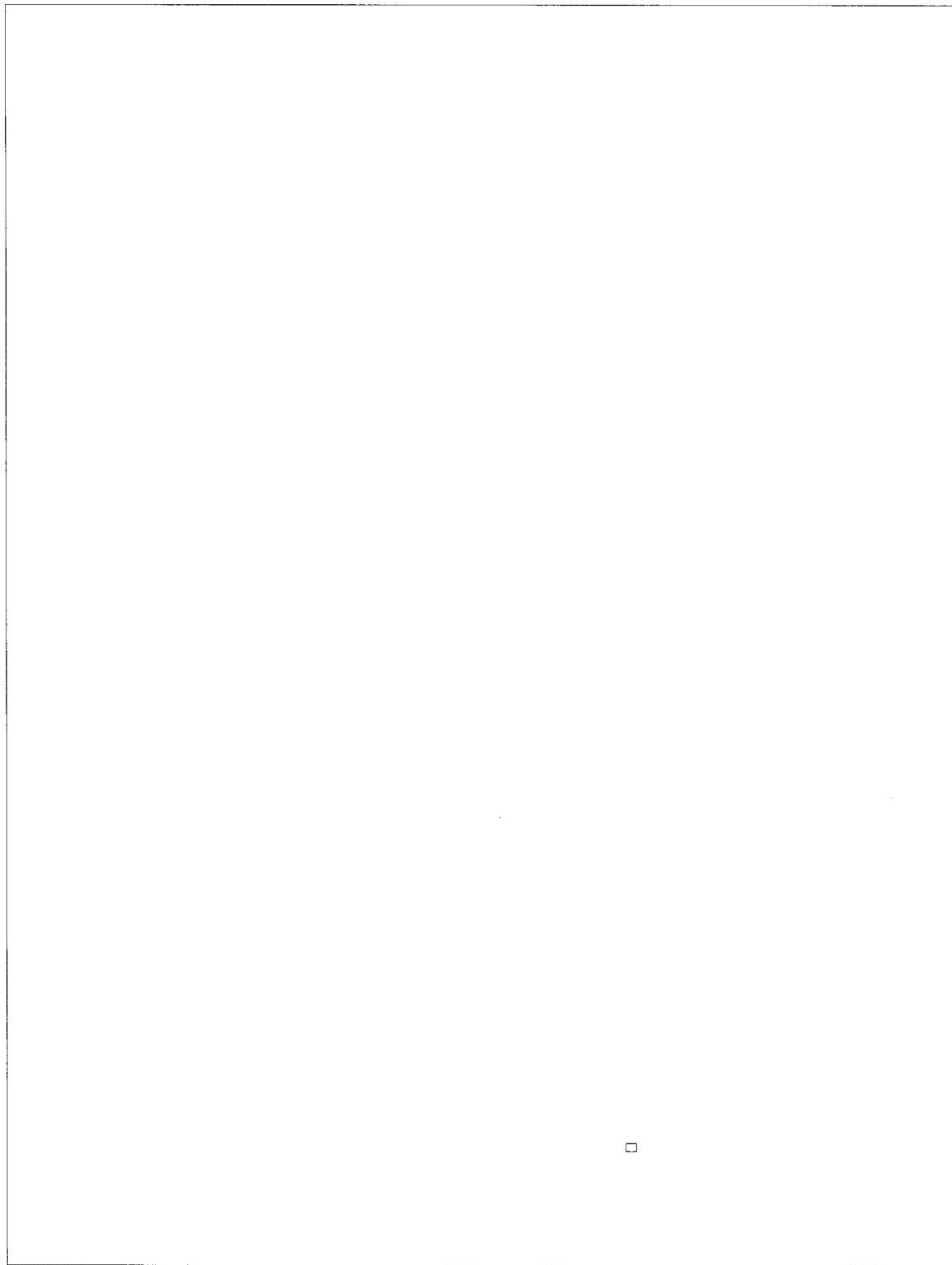


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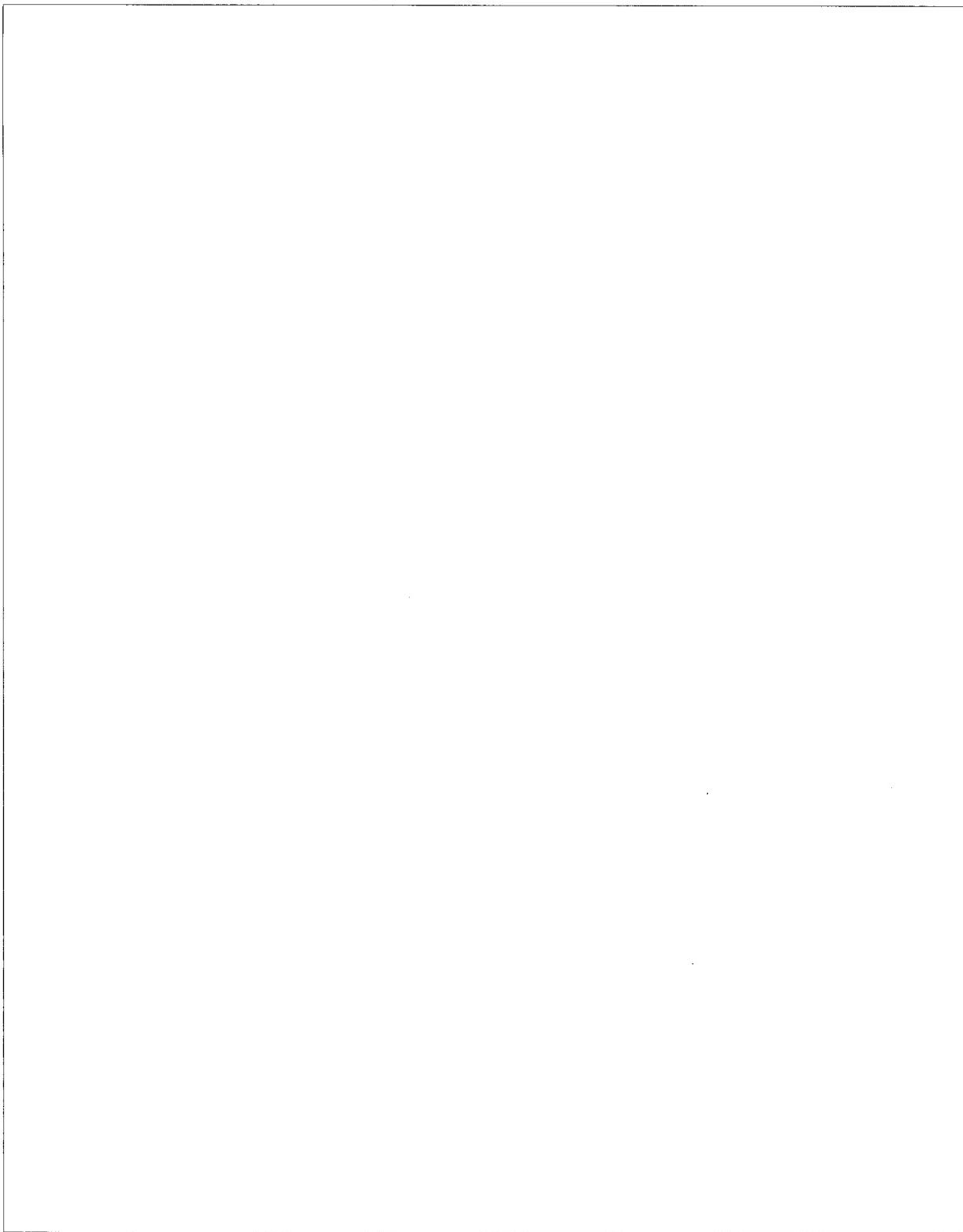
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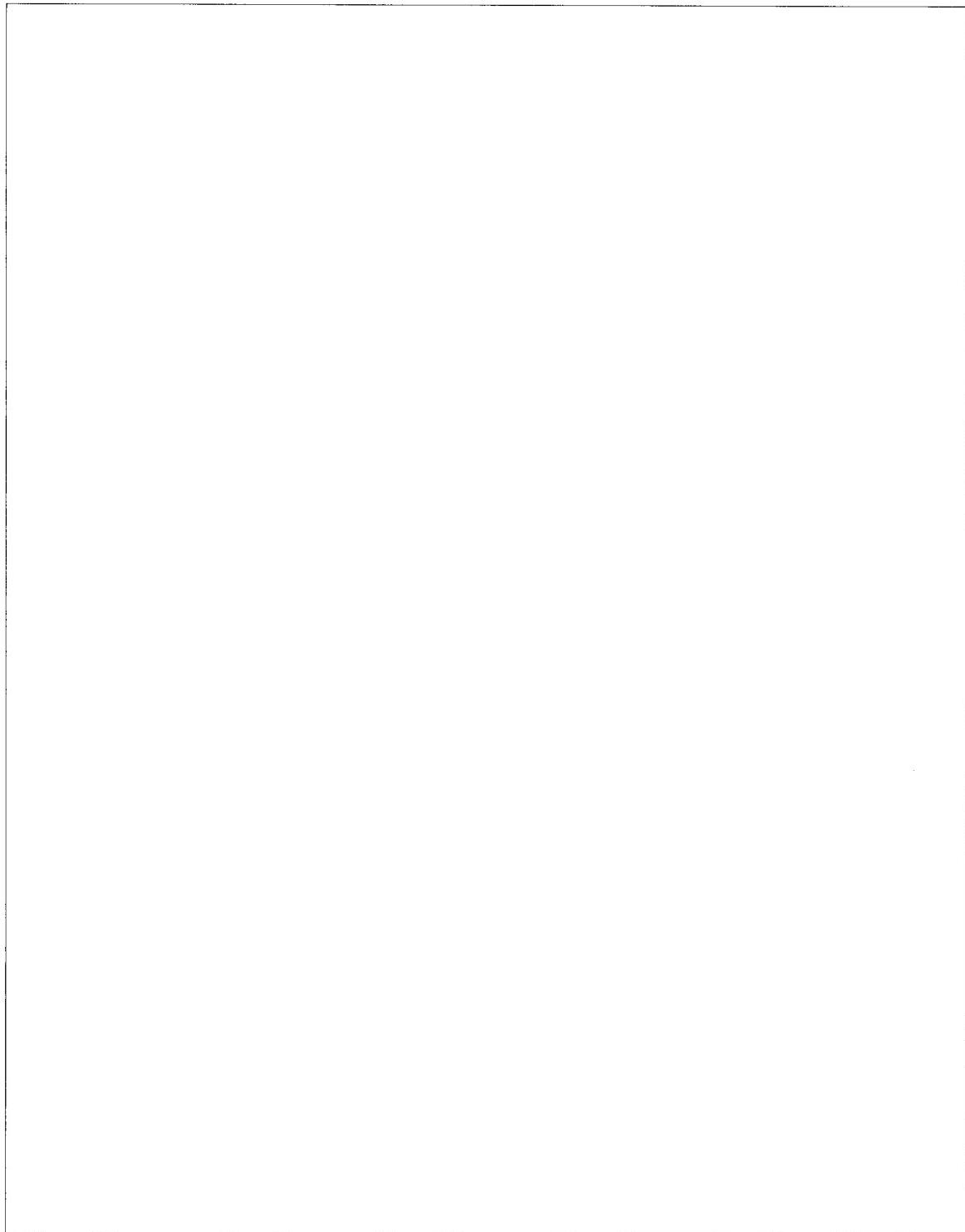


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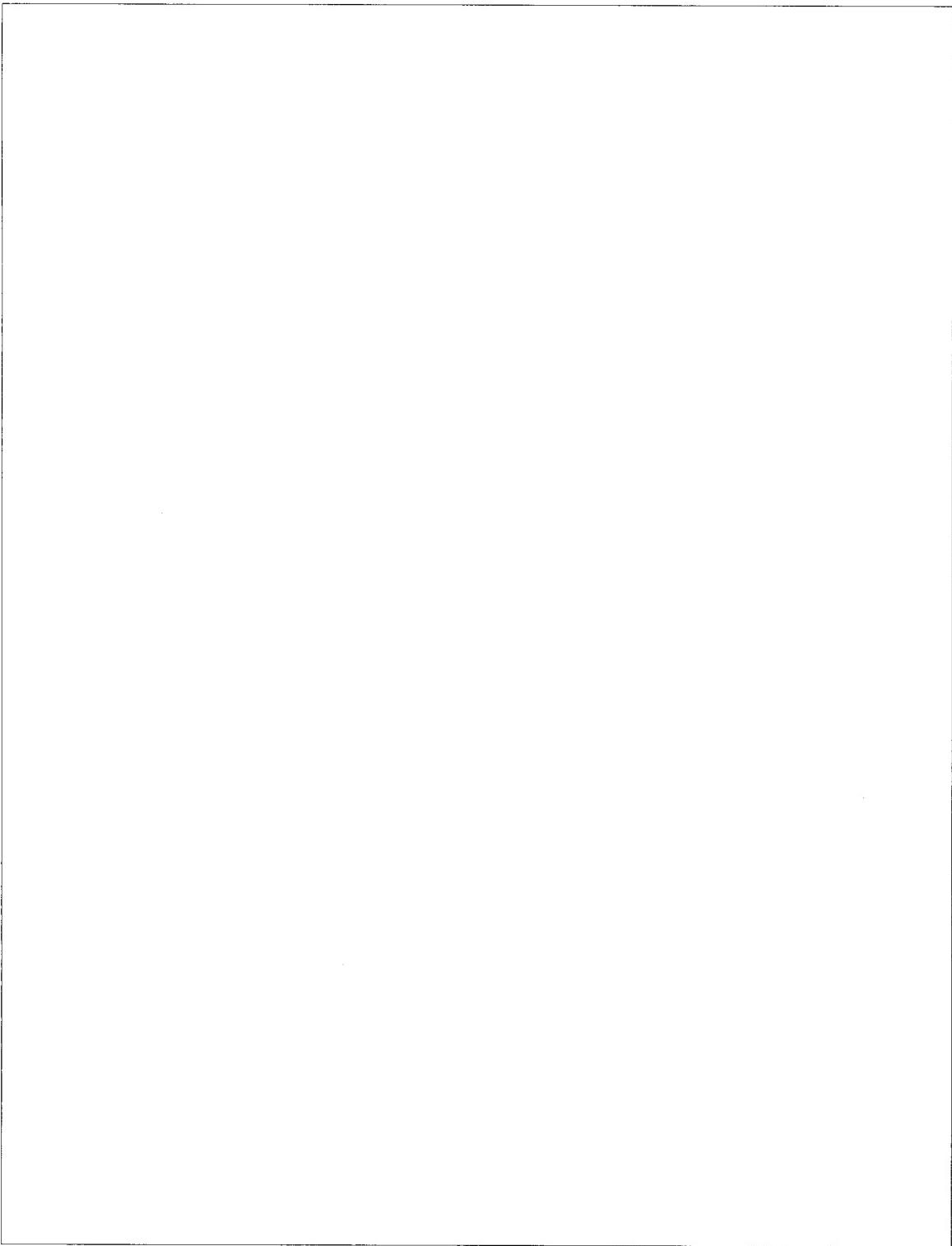


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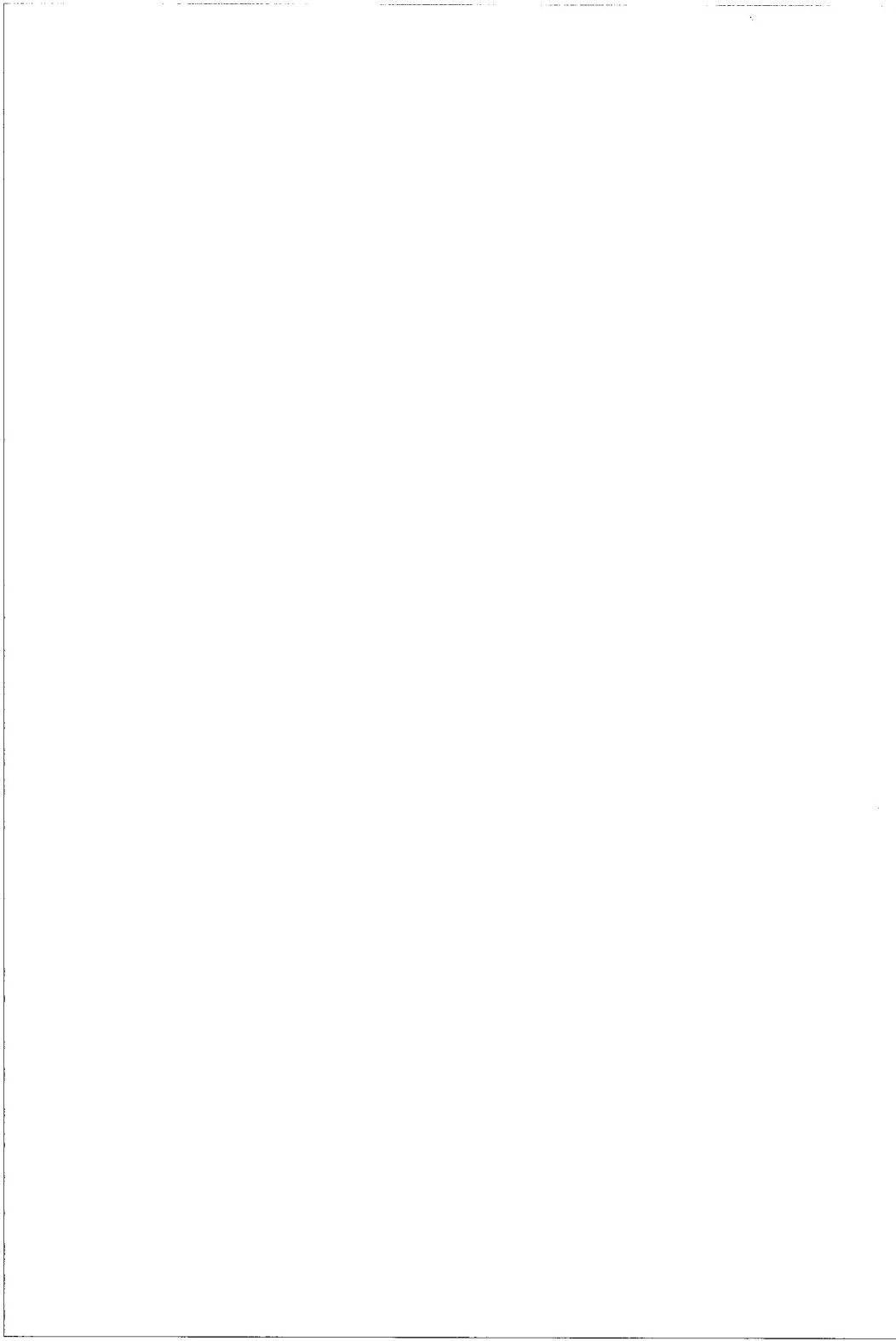


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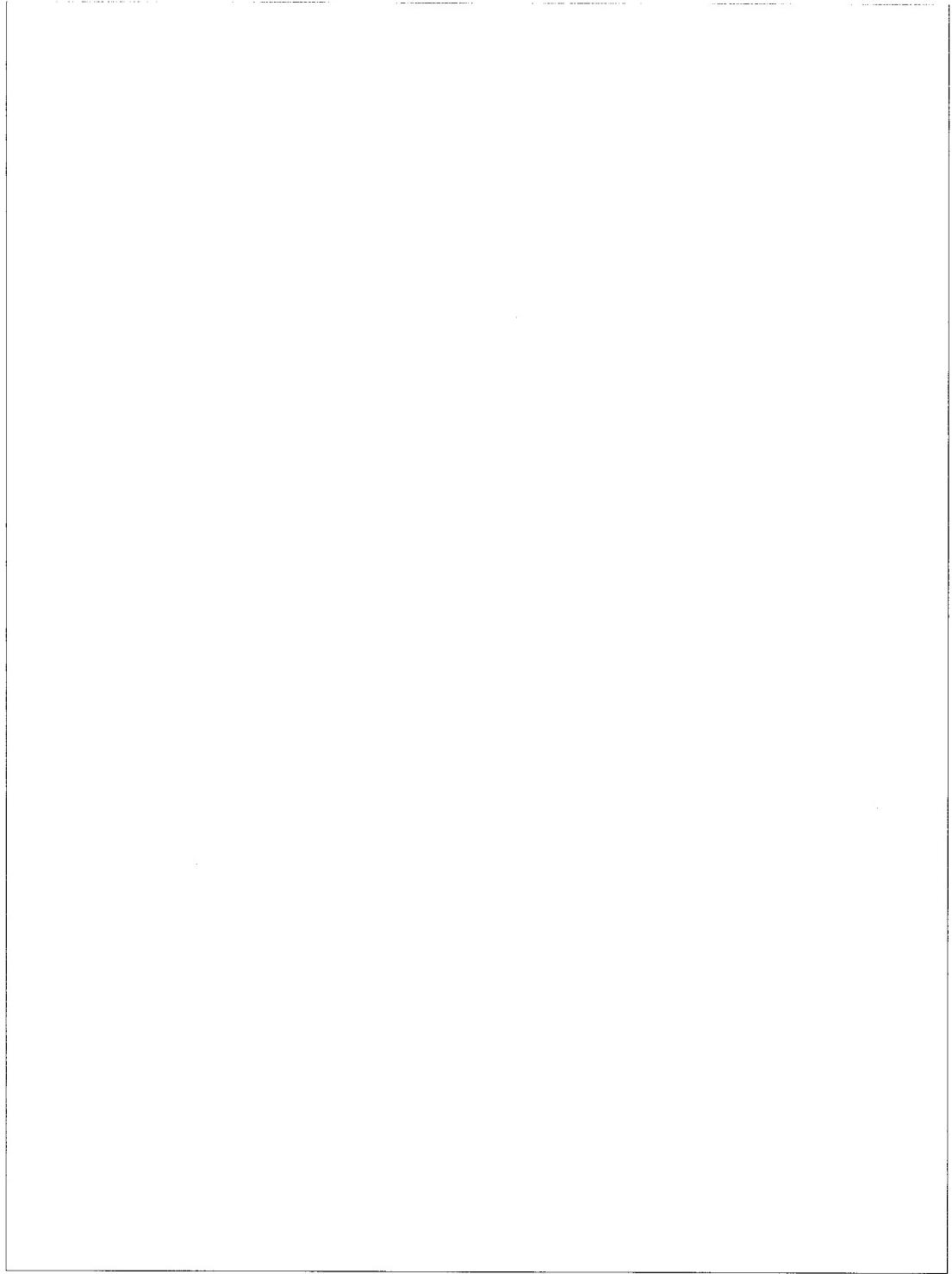


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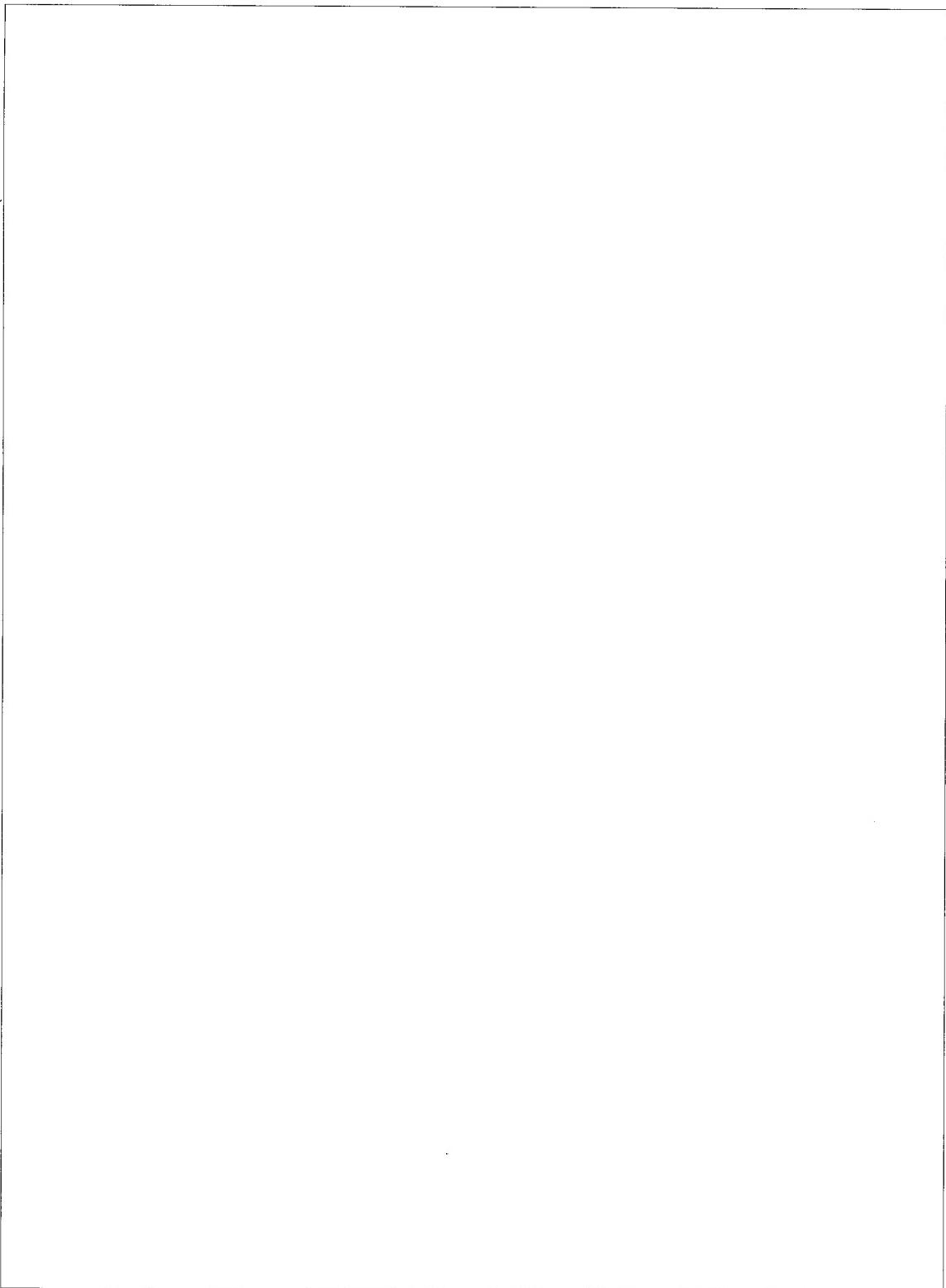


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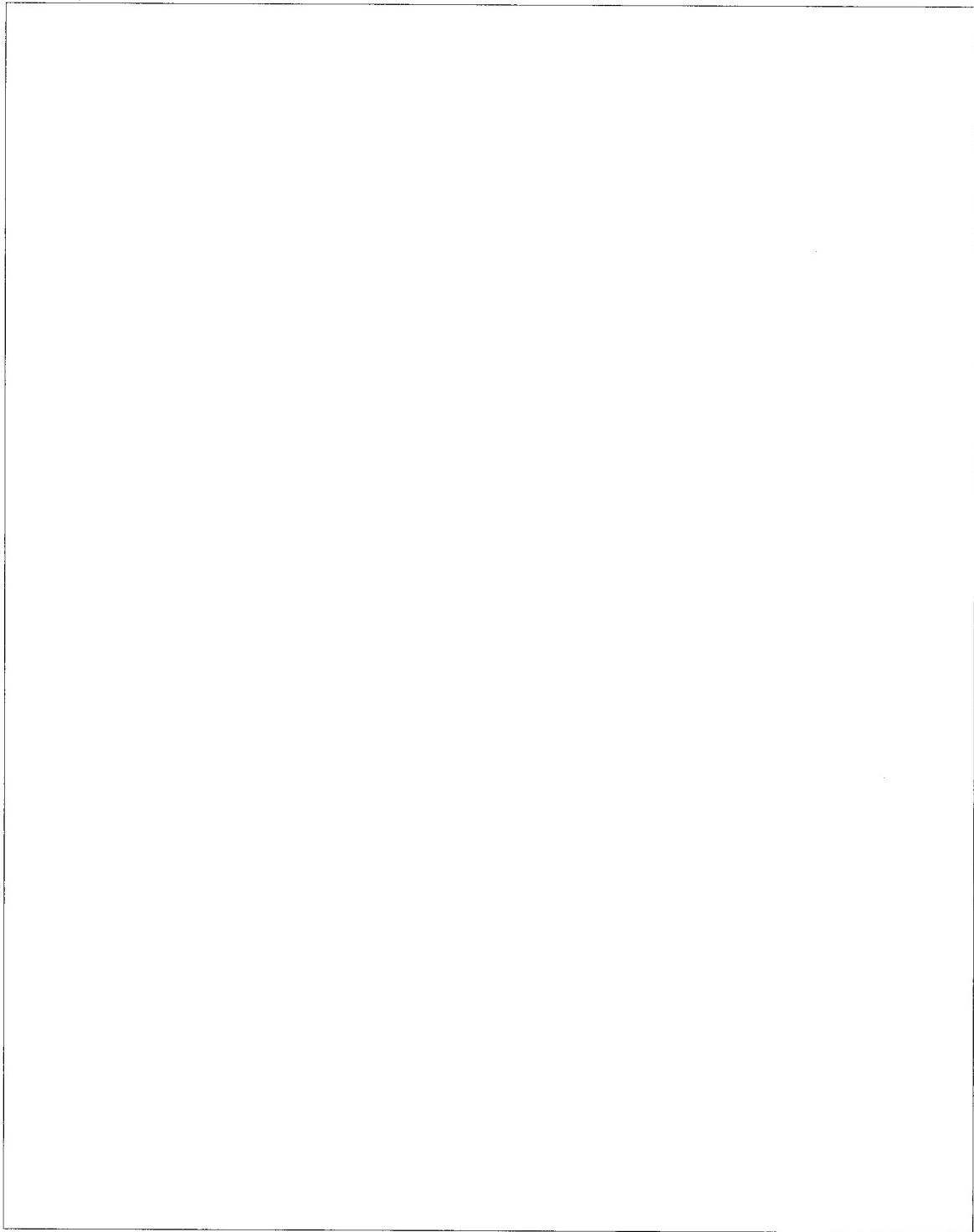


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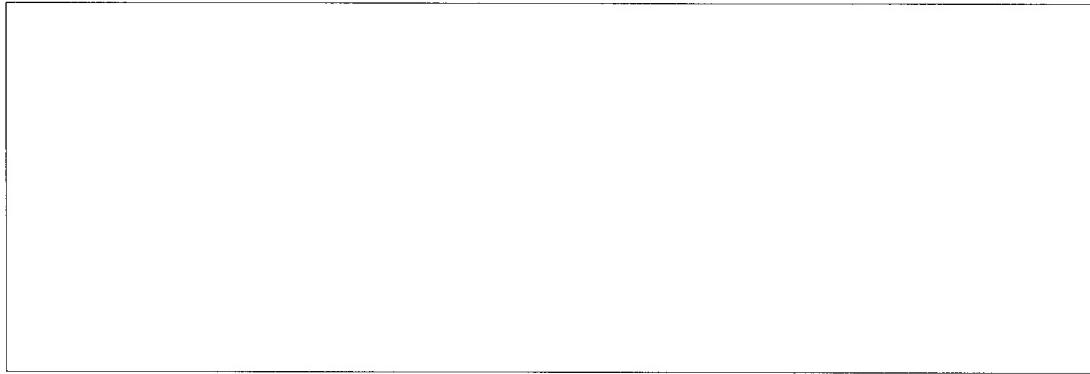
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This account of Audit Staff experience relative to [redacted] is presented not only to document the audit function [redacted]  
[redacted]

but also to emphasize the unlimited operational environment of staff auditors. During the periods of crises in Europe, the Middle East, Africa, the Western Hemisphere, and Southeast Asia, Audit Staff continued the routine examination of custodial practices and controls over the use of Agency resources unless requested to defer audits due to unusual operational circumstances. That such requests were rare is indicative of the recognition of the value of audit as an objective appraisal of management activities at field as well as Headquarters levels.

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In the performance of audits under circumstances such as those encountered with [redacted]  
[redacted] or in audits of Vietnam Station and [redacted]  
[redacted] auditors shared for brief periods the same hardships and hazards experienced by Agency or military personnel assigned to the operations audited. This created an empathy with field activities and personnel not ordinarily available to auditors in the normal government establishment, and incidentally enhanced the protection of Agency resources through the knowledge by Agency personnel that, regardless of location or circumstances, they were subject to audit.

During the period from 1962 through 1967 the last of the auditors retired who were trained in the now obsolete method of detailed voucher review. While this had little effect on the progress of audit policies and programs which had evolved in furtherance of modern techniques, the departure of dissenting auditors provided a spirit of unanimity to the audit effort.

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In connection with several organizational changes made by John A. McCone as Director of Central Intelligence, the Audit Staff was transferred from the Support Directorate to the Office of the Inspector General on 20 March 1962.<sup>94/</sup> This transfer recognized the need for complete independence of the Audit Staff from activities and organizations subject to audit and the expanded responsibility of the Staff as a managerial reporting medium.

[redacted] as a member of the immediate staff of the Inspector General, was in a position to coordinate the investigative and survey work of the Audit Staff with that of the Inspection Staff, and with the concurrence and encouragement of [redacted] who was appointed Inspector General on 2 May 1962,<sup>95/</sup> audit and inspection of the Far East Division in January 1964 was conducted jointly, with members of the Audit Staff FE Field Branch serving as both inspectors and auditors. In other instances, auditors were detailed to inspect cases of suspected defalcation of official funds at [redacted]

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[redacted] in lieu of a member of the Inspection Staff. Coincidentally, this cooperation between auditors and inspectors was anticipated by Admiral Hillenkoetter in his instructions to the Executive for Inspection and Security in January 1948:

Upon conclusion of audit inspection of unvouchered funds<sup>7</sup>, auditors will accompany inspectors on such trips as their presence may be needed.<sup>96/</sup>

During 1962 and 1963 the emphasis placed on counterinsurgency efforts within the government resulted in the Agency acquisition and operation of [redacted] aircraft operating companies, [redacted]  
[redacted]

[redacted] These facilities,

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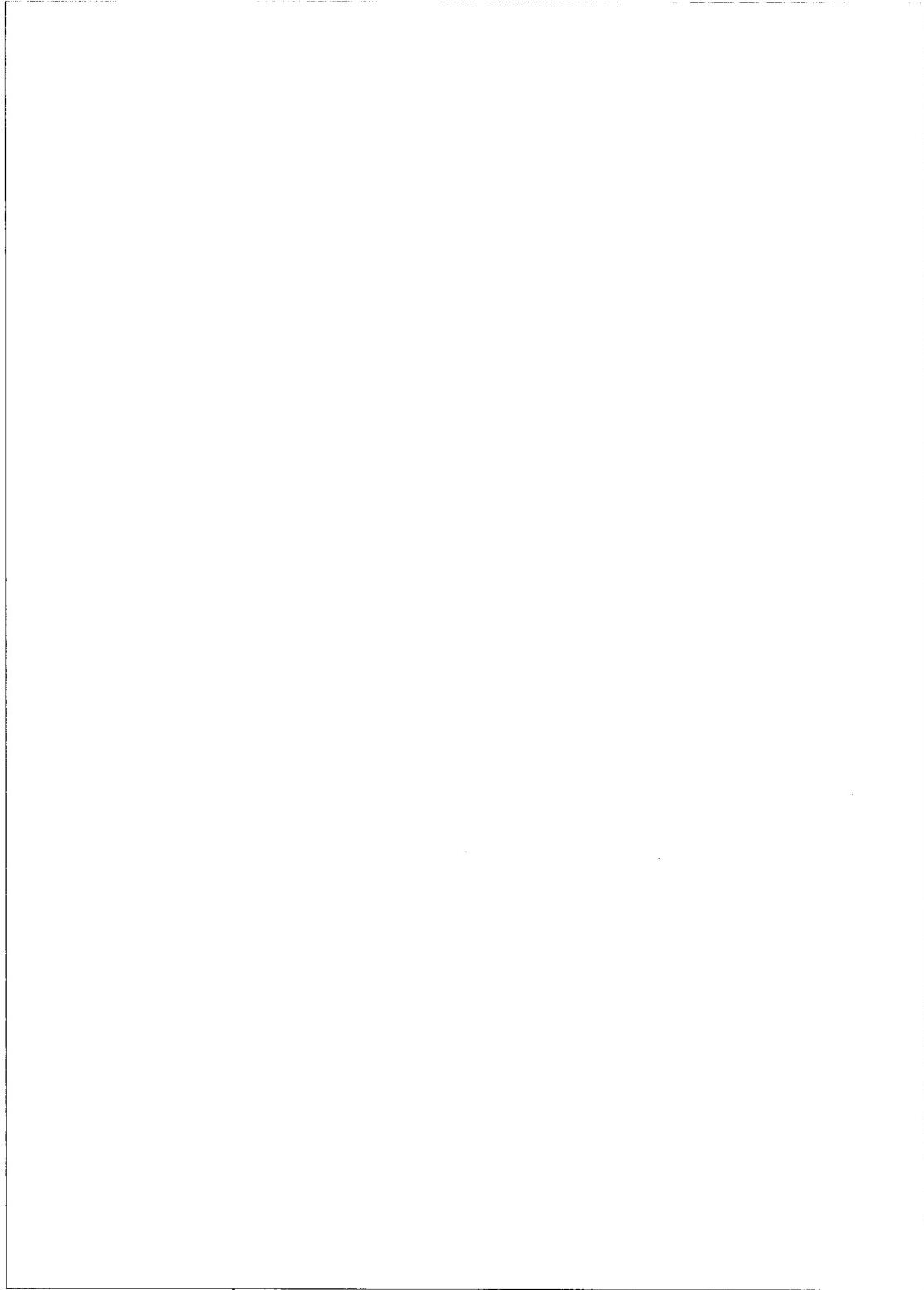


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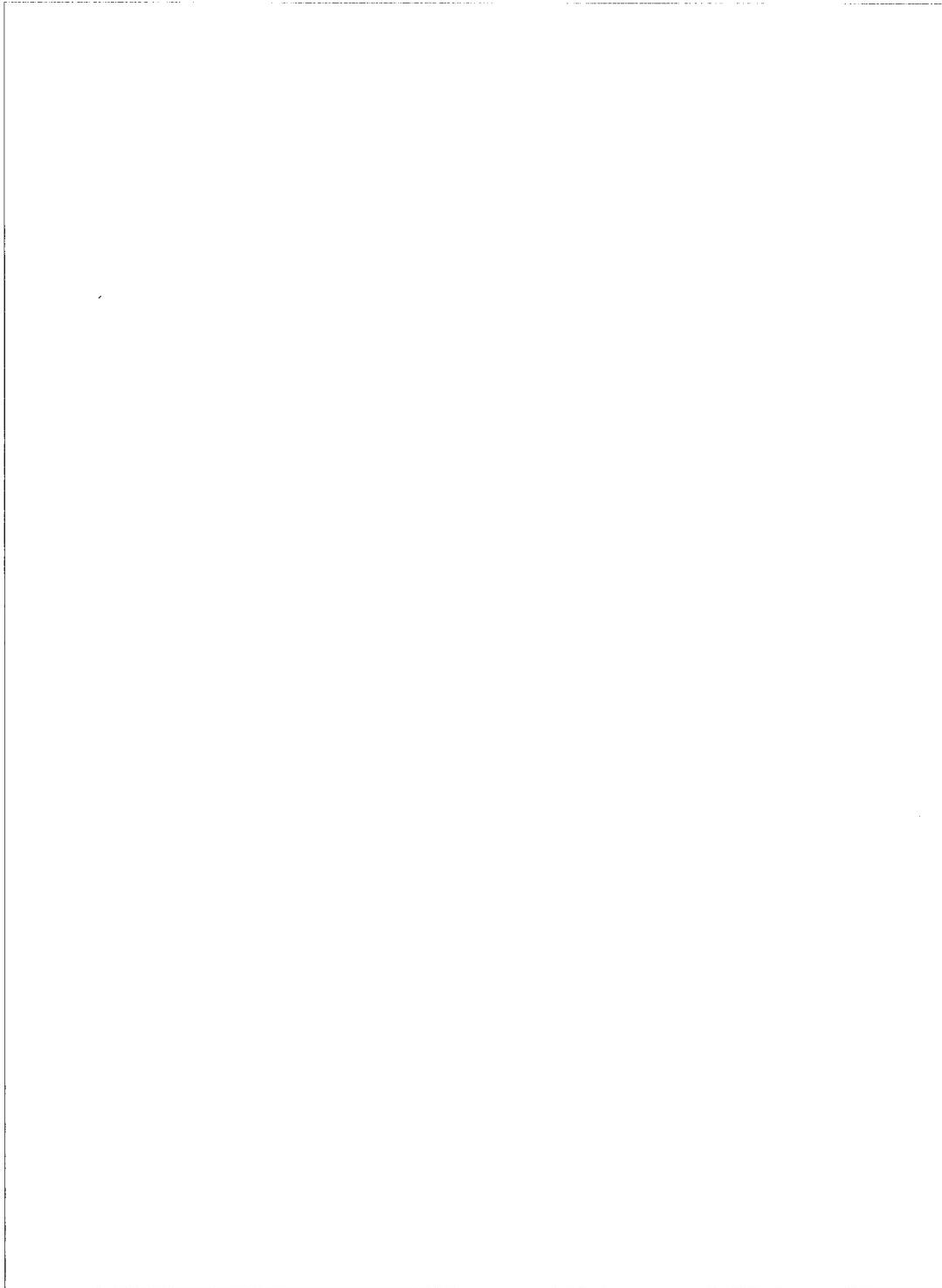


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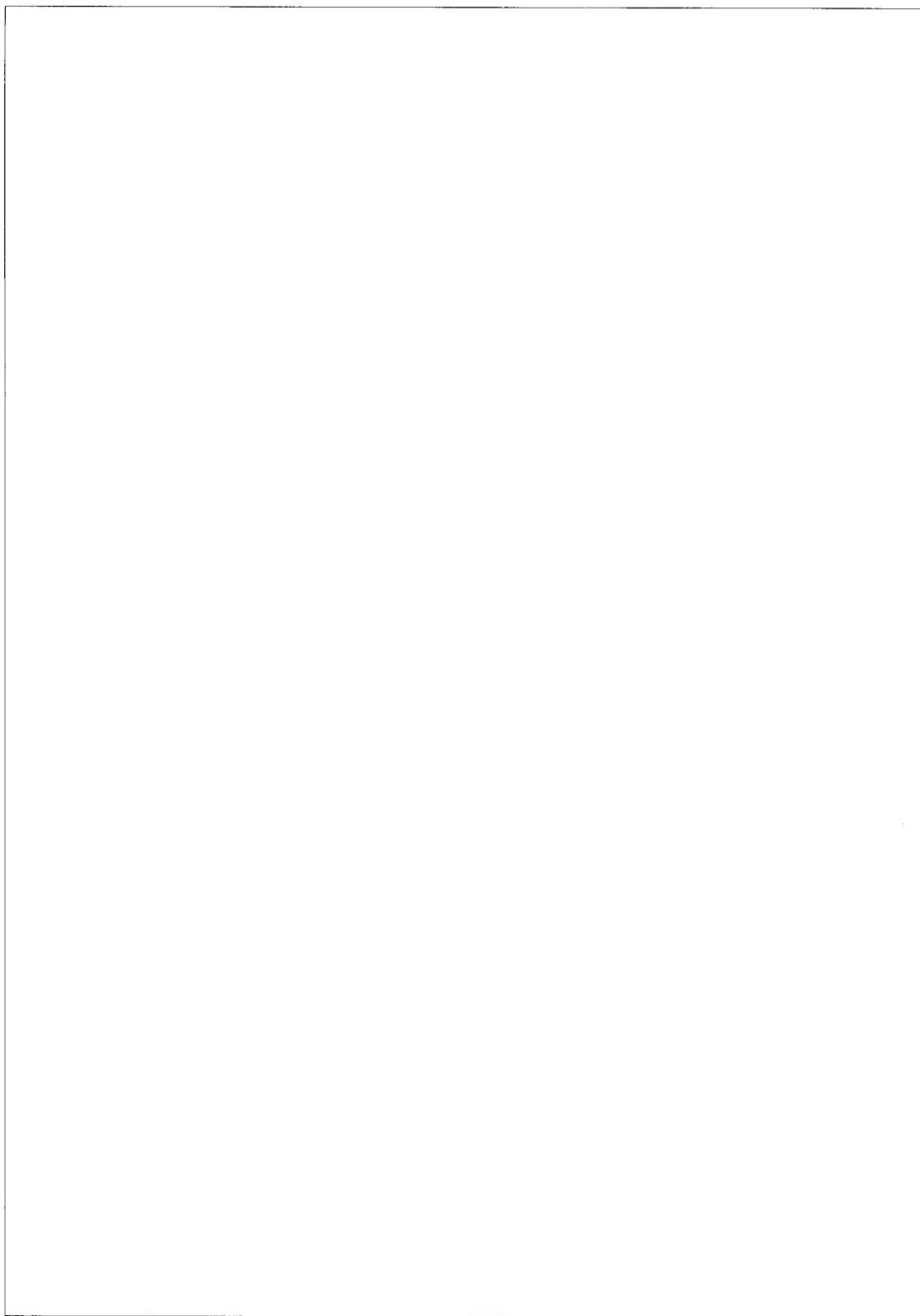


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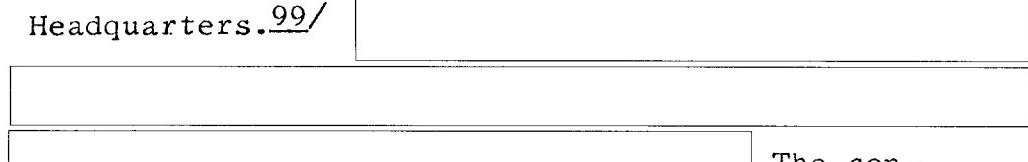


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In early 1961, the flow of United States resources to foreign countries as a result of the adverse balance of trade and the cost of the large government establishment abroad required re-evaluation of the need for certain categories of Agency personnel in the foreign field. Field auditors, who did not contribute directly to the intelligence mission overseas, were among those whose need was questioned. In June 1963, in response to a verbal inquiry by the Executive Director-Comptroller, the Chief, Audit Staff submitted an estimate of the consequences of the closing of the Staff field branches and the conduct of field audits from the Headquarters.<sup>99/</sup> [Redacted]



[Redacted] The conclusion of this study was that an effective field audit program could be conducted from Headquarters if necessary, with little additional cost. The

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counter-argument was submitted, however, that intangibles such as accessibility, effectiveness as related to familiarity with operations under audit, promptness of reporting, and recruitment incentives would all be adversely affected if overseas audit offices were closed. On the basis of these cogent arguments, the Audit Staff field branches,

[redacted] were

[redacted] allowed to remain in place until the Balance of Payments (BALPA) and Overseas Personnel Reduction (OPRED) programs of 1968 and 1969.

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~~SECRET~~VI. Synopsis

Thus, by 31 December 1967, the goal envisioned by [redacted] in 1951 had been reached.

The Agency policy with regard to audit was formally stated in [redacted] as

The Agency shall provide audit facilities and services to ensure the highest possible protection of government assets consistent with security limitations necessitated by the nature of Agency operations.<sup>100/</sup>

Execution of this policy was the mission of the Audit Staff, which was organizationally a part of the Office of the Inspector General. The Staff at the end of 1967 consisted of about [redacted]

[redacted] Auditors assigned to

the Staff had developed a noteworthy level of experience and professional competence. Of [redacted] auditors, more than half had accumulated an average of 10 years' experience in the auditing of diverse Agency activities, and approximately [redacted] percent

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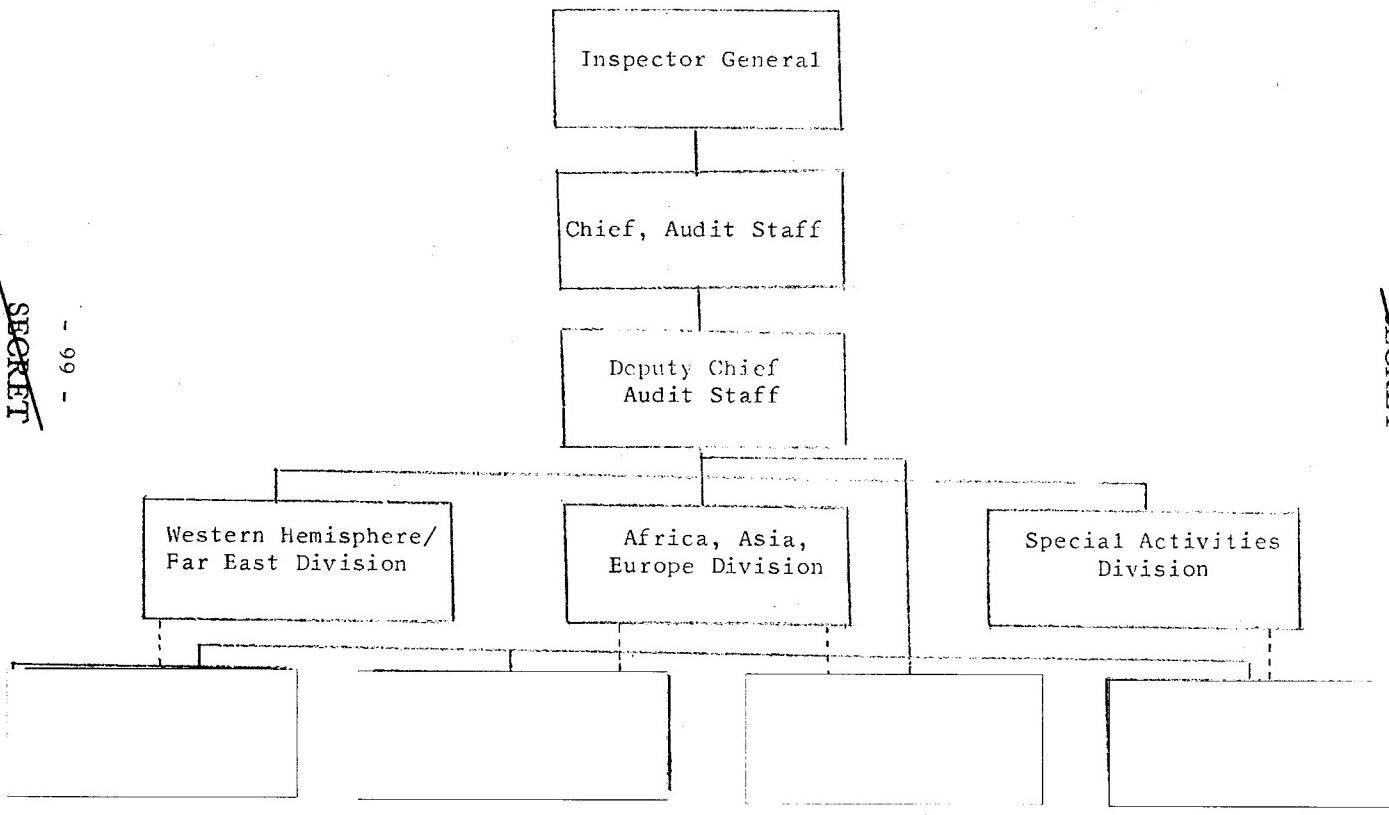
were licensed as certified public accountants. The

Through these staff components, audits were conducted of all Agency installations and activities approximately every twelve months. Audit policy, procedures, and standards were formalized in a Handbook for Auditors and in audit work orders specifically designed to assure adequate audit coverage of each Agency activity. Audits were performed in accordance with professional standards established by the American Institute of Certified Public Accountants and the Institute of Internal Auditors. Findings of audits were documented in audit workpapers and reported through the Inspector General to the Executive Director and responsible management officials. Recommendations for corrective action resulting from audits were routinely well received and adopted by Agency management. Auditors were welcomed by all Agency personnel, who had

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Audit Staff Organization Chart  
31 December 1967

Figure 5



— = Supervision and policy direction

----- = Headquarters coordination and liaison

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grown to accept audit as a routine and constructive review on behalf of the highest management. In calendar year 1967 the Staff completed [ ] audits, almost equally divided between Headquarters and foreign field activities.<sup>101/</sup>

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~~SECRET~~Appendix A. Chronology of Significant Events  
1 July 1947 - 31 December 1967

- 1 July 1947 Provision is made for Audit Division, Inspection and Audit Branch, Office of Inspection and Security.
- 16 November 1947 First auditor is employed.
- 16 December 1947 DCI, Admiral Hillenkoetter, directs that first audit be undertaken.
- November 1948 Audit Division is expanded to Audit Branch of EIS.
- 13 July 1948 Strength:  employees.
- 1 December 1950 Property audit is assigned.
- 20 February 1951 Strength:  employees  
(Authorized: )
- 18 April 1951 Reorganization - Audit Division, EIS becomes Audit Office of DDA.
- 18 January 1952 Position of Auditor-in-Chief is established.
- 20 February 1952 Strength:  employees.
- 1 September 1952 Proprietary audits are transferred from Controller's Office.

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October 1952

6 January 1953

Strength: 

May 1953

August 1953

May 1954

16 February 1955

Audit Office is designated as Audit Staff, and Headquarters group as Headquarters Audit Division with General, Proprietary, and Property Audit Branches.

21 November 1955

Strength: 

30 November 1955

T/O's of field units are transferred from DDP to Audit Staff world-wide T/O.

18 January 1957

Office of Deputy Chief, Audit Staff is established.

9 August 1957

Strength:  (ceiling).

3 February 1959

Field Audit Division is established under Deputy Chief, Audit Staff.

1 February 1960

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15 August 1960	[ ] becomes Chief, Audit Staff.
23 June 1961	Audit Staff is reorganized into geographical divisions. [ ]
1 July 1961	[ ]
20 March 1962	Audit Staff is transferred to Office of Inspector General.
June 1962	GAO withdraws from CIA.
16 June 1963	Proposal is made to conduct field audits from Headquarters as an economy measure.
January 1964	[ ]
1 July 1964	[ ]
1 January 1967	[ ]
31 December 1967	[ ]

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